THESIS OF DOCTORAL (PhD) DISSERTATION

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University Doctoral (PhD) Dissertation Abstract

FRAUD RULES IN THE LETTER OF CREDIT LAW: AN ANALYSIS OF INTERNATIONAL REGULATIONS AND NATIONAL LAWS WITH PROPOSED AMENDMENTS FOR VIETNAM

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UNIVERSITY OF DEBRECEN
MARTON GÉZA DOCTORAL SCHOOL OF LEGAL STUDIES

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DECLARATION ON CONFORMING TO RULES ON PREPARING THESIS

I, the undersigned Bui Le Thuc Linh (Neptun-code: C9AFCS) by signing the present statement declare that the thesis, entitled

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Bui Le Thuc Linh

SUPERVISOR'S RECOMMENDATION

Bui Le Thuc Linh's doctoral dissertation fills a gap. The subject of this dissertation is fraud rules in the letter-of-credit law. International business always has higher risks than domestic business. Due to the unreliability between parties, documentary credit was fashioned by mercantile usage. The documentary credit removes the risk for not being paid of the seller as well as makes sure the buyer does not have to pay money until a set of documents whose title demonstrates the ownership of the cargoes presented to the bank-third party. This institution is spreading more and more widely. Therefore, it is particularly important to analyze the topic in a way that can be used for law enforcement.

The candidate fulfilled his task excellently. The part that fully presents the justification of the choice of topic and the application of research methods is followed by the definition of hypotheses and the clarification of basic concepts. In the substantive part, which is sufficiently founded in this way, the author tries to make all significant legal institutions of the discussed topic the object of investigation in a problem-oriented manner by depicting wide-ranging practical experiences and with a complex outlook. He constantly strives to present solutions that can be used in all legal systems. On the basis of the consistent structure, it is possible to explain the concluding thoughts summarizing the results of the research.

References are consistent, the literature used is extensive. It follows that he separates his own thoughts, justifying the thorough research work, from the sources of legal literature. The correctness of the text is impeccable. The topic of the dissertation contains scientifically evaluable, authentic data and results. Both in terms of content and form, it meets the expectations of PhD dissertations in law, and – attention to the workplace debate – I recommend that it be submitted for public defense.

Debrecen, April 27, 2023.

dr. Pribula László

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I would be negligent if I do not thank my parents for their everlasting tolerance. Their confidence in me has sustained my enthusiasm and encouraged me throughout my academic journey. And as absurd as it may sound, I would like to express my heartfelt appreciation for the hard work, dedication, and perseverance I have put into this thesis. It has been a long and challenging journey, but I am proud of the effort and commitment that I have shown throughout the process. None of this would have been possible without me. My contribution and effort have been essential for achieving this accomplishment.

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ABBREVIATIONS

ABBREVIATION	EXPANSION
BIMCO	Baltic and International Maritime Council
C.I.F	Cost, insurance, and freight
C.I.P	Carriage and Insurance Paid To
CMI	Committee Maritime International
CPL of PRC	Civil Procedure Law of the P.R.C
eUCP	Supplement to the Uniform Customs and Practice for Documentary Credits for Electronic Presentation
FIATA	International Federation of Freight Forwarders
GFE	Glass Fibers and Equipment Ltd.
ICC	International Chamber of Commerce
ICS	International Chamber of Shipping
IFSA	International Financial Services Association
ISBP	International Standard Banking Practice for the Examination of Documents under Documentary Letters of Credit
ISP 98	International Standby Practice
NCCUSL	National Conference of Commissioners on Uniform State law
P.R.C	People's Republic of China
RBC	Royal Bank of Canada
SPC of PRC	Supreme People's Court of P.R.C
SWIFT	Society for Worldwide Interbank Financial Telecommunications
UCC	Uniform Commercial Code
UCP	Uniform of Customs and Practice for Documentary Credits
UNCITAD	United Nations Conference on Trade and Development
UNCITRAL	The United Nations Commission on International Trade Law
UNIDROIT	International Institute for the Unification of Private Law
URDG	Uniform Rules for Demand Guarantees

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Introduction

a. Analysis of the topic

This thesis intents to give a brief introduction to the unique utility of letters of credit, which specifically focus on commercial letters of credit, and introduce the inadequacies in the system of letters of credit concentrating on fraudulent activities and presenting the shortage of justice in regulating such areas in Vietnam. The rights and obligations of parties in the transactions of commercial letters of credit will be described in this thesis as well as the cornerstone rules of letters of credit. The thesis will exhibit the exercise of unscrupulous parties misleading documents and obtaining payments without performing duties. Such fraudulent activities illustrate circumstances that jeopardize the stability of the documentary credit system.

This dissertation also emphasizes the official regulations dealing with such fraudulent activities in some specific countries as well as the opinions of their courts. The dissertation then shall further mention the recent economic situation of Vietnam regarding the application of commercial letters of credit, including the current regulations and the recent legal judgments. The lack of law in this field in Vietnam is also expressed through this study by presenting the recent decisions and the Vietnam case law. This case law shall perform the point of view of the Vietnam People's Courts toward fraud in letters of credit as well as the right and duties of parties. Then, the author shall try to give recommendations based on the current situation in Vietnam.

b. Reason to choose the topic

The letter of credit is the accomplishment of international merchants. Besides the main function is to be assisting the progress of international commerce, the letter of credit also brings profit to the banks. However, the letter of credit is not created to prevent fraud within it. The fraud trend is considered to start in 2001 (Byrne, 2002, p. 28), and ever since then, along with the development in technology, fraudsters are becoming more sophisticated. Through years of implementing letters of credit, there have been several fraudulent activities reported by the International Maritime Bureau such as the case where 400 million US dollars of metals business of United Arab Emirates (Solo Industries UK Ltd v. Canara Bank, 2001) or the loss of 200 Million US dollars of a single bank (ICC Commercial Crime Services, 2002, pp. 26-28).

In the current situation in Vietnam, the economy is growing up in recent years. From the period 2015 to 2020, the total exports and imports have grown by 217 526,4 million US dollars more. In 2020, the exports had reached 282 6278, 90 million US dollars. The higher development of the economy, the bigger demand for using financial services to set up settlements for international transactions. Letters of credit are parts of financial services including payment provision using bank accounts in Vietnam which also illustrate a positive scenario. To be specific, the number of imported financial services in 2019 reached the highest point in the

period 2015-2020 which is 309 million US dollars. In recent years, the demand for using financial services in Vietnam is becoming larger and so is the demand for using letters of credit.

Together with the growth of the economy, there have been several reports relating to fraudulent activities in letters of credit in Vietnam. In 2016, several exporting companies reported the loss of thousands of US dollars because of fraud in commercial letters of credit (Vietnam Association of Seafood Exporters and Producers, 2016, p. 4). According to Vietnam Export and Processing Association, in 2015 - 2016, Vietnamese companies lost 8 billion US dollars mostly due to fraudulent activities (Nguyen Trong Thuy, 2019). Due to such situations, the Vietnam Supreme People's Court published a case regarding fraud in letters of credit in the book of Vietnam case law and made further comments to guide the merchants and Vietnam People's Courts in ruling the cases relating to the letters of credit, especially commercial letters of credit.

As has been stated, such situations have shown a serious gap in the letter of credit law. This fraud situation is not handled by the main source of international regulations which is the Uniform Customs and Practice for Documentary credits since fraud is considered a domestic problem. Hence, some countries have tried to govern their national letters of credit as well as embed fraud rules to manage fraudulent activities. In this thesis, the author will try to introduce and examine fraud rules from both international and national sources. Then the author shall analyse the situations in the Vietnamese legal system, explain the modest sample case law, and adopt a personal perspective that focuses on issuing a domestic regulation for fraudulent activities in letters of credit in Vietnam.

c. The subject of the research

The subject of this dissertation is fraud rules. Letters of credit have two kinds which are commercial letters of credit and standby letters of credit. Even though both kinds of credit are based on the documents, commercial credit is different to standby one. The main function of commercial credit is to provide payment for goods based on a set of different documents. Meanwhile, standby credit also requires for document presentation, however, such documents are simple like a request to the bank to pay for the non-performance of the applicant. Hence, the standby letter of credit is considered a guarantee for the buyer's performance. Due to the complicated documents presented in the commercial letter of credit that makes the commercial letter of credit vulnerable to fraudulent activities, this thesis shall focus on fraudulent activities in commercial letters of credit. However, during the development of standby letters of credit, fraud in the standby letters of credit had undergone a significant change, which imposed a great impact on the fraud rules. The regulations regarding the fraud rules for standby letters of credit are quite noticeable, hence, the author will further mention some specific cases and regulations relating to standby letters of credit to contribute a better view of the general fraud rules in letters of credit.

The regulations governing fraudulent activities in letters of credit shall be examined under the scope of international law as well as national law. The legislation of Vietnam regarding fraud

in letters of credit, especially in commercial letters of credit, is also investigated in this dissertation, including the related laws and case law. The orientation of the Vietnam People's Courts as well as the recommendation of the Vietnam Supreme People's Court shall be illustrated in this work.

d. Scope of the topic

The scope of the topic will include a comprehensive analysis of relevant international and Vietnamese laws and regulations, as well as case studies and empirical data to support the proposed amendments to the current Vietnamese legal framework. Additionally, the thesis will explore the impact of fraud rules and their integration into value chains. Besides international regulations, the author shall focus on the national uniforms regulating fraud rules. For example, the United States regulations regarding fraud rules which is the Uniform Commerce Code will be embodied in this thesis. Furthermore, the regulations and case law of the People's Republic of China relating to fraud rules are also illustrated and examined in this thesis. Additionally, the law of Vietnam and the specific case law will be clarified as well.

Besides the typical UCP, the eUCP 2.0 which came into effect in 2019 and is used to govern the electronic presentations of the letter of credit shall be briefly mentioned in this thesis but will not be well addressed since, after the eUCP version 1.0 is issued, the percentage of the e-trade business still constitute less than 1% of the finance field (Godier, 2000). Electronic documents are not strongly believed to make a compelling profit until a few years later (Godier, 2000) (Katsman, 2002, pp. 16- 17) (Barnes & Byrne, 2001, p. 33). The projects investing in the online system are processing based on the development of blockchain technology, but they are still in their first steps. In the processing of the credit in the e-transactions, all parties should be merged in the same stage. Hence, the buyers, sellers, and banks should be registered and authenticated before any transactions start (Katsman, 2002, pp. 16- 17). Due to this progress, there is nearly no legal framework to handle the legal paper works, hence, the eUCP is considered to bloom in the far future. Hence, it is precluded from this study.

e. Legal issues

Letters of credit have been created for years and there are numerous scholars in this field have identified certain inadequacies in the system of letters of credit such as the high standards in proving the conforming of the presented documents which form obstacles for the sellers and builds platforms for the buyers to use this kind of barrier to enjoin the payment of the credit while this process should not be enjoined, the absence of the right and duties (Buckley, 1996, p. 217), the defenceless of the buyers' positions under the credit (Mann, 2000, p. 2525) and the most important issue, fraudulent activities. These problems show a lack of consideration for a sensitive situation in the progress of letters of credit; however, the Vietnam Legal System has paid little attention to such issues. None of Vietnam's regulations has set out a detailed picture of the letter-of-credit system and classified the provisions to regulate fraudulent activities which are increasingly high in the current economic situation of Vietnam.

The author has set the main question **"What are the legal solutions to protect Vietnamese merchants from fraudulent activities in letters of credit?"**. Based on such question, the author deprives a hypothesis for this study "Implementation of legal measures to protect Vietnamese merchants from fraudulent activities in letters of credit can lead to a reduction in financial losses for the parties involved and enhance the integrity and reliability of the payment system." Based on the such hypothesis, the author has derived three potential hypotheses that may lead to legal solutions to protect Vietnamese merchants from fraudulent activities in letters of credit.

The first hypothesis suggests that the interpretation and verification of documents in a letter of credit rely heavily on the expertise and trustworthiness of intermediaries such as banks and shipping companies, which may reduce additional risks and uncertainties in the payment process in sales contracts.

The role of intermediaries such as banks and shipping companies in the letter of credit payment process is critical for ensuring the accuracy and completeness of the documentation required for payment, as well as for providing assurance and confidence to both the buyer and the seller that their interests are protected. The expertise and experience of intermediaries in the letter of credit payment process can help to identify and mitigate potential risks and errors in the documentation, such as discrepancies or inconsistencies, which may result in delays or even rejection of payment. The trustworthiness and reliability of intermediaries in the letter of credit payment process depending on various factors, including their reputation, track record, compliance with regulations and standards, and their ability to adapt to changing market conditions and technological developments.

The second hypothesis suggests that national laws play a dominant role in defining fraud rules, reflecting the unique legal and cultural contexts of each country. International regulations serve mainly as guidelines for cooperation and coordination among different authorities.

The legal and cultural diversity among different countries implies that fraud rules should be tailored to the specific context of each jurisdiction, taking into account factors such as the legal system, the business environment, and the level of institutional capacity and trust. The predominance of national laws in defining fraud rules highlights the importance of domestic regulatory frameworks and law enforcement mechanisms in preventing and punishing fraudulent activities. The existence of international guidelines and best practices for fraud prevention and detection can facilitate the coordination and collaboration among different authorities and stakeholders involved in international transactions, promoting the convergence and convergence of fraud rules across different jurisdictions.

The third hypothesis suggests that the implementation of clear and consistent fraud rules in Vietnam can help to deter and detect fraudulent activities related to letters of credit, thereby enhancing the integrity and reliability of the payment system and reducing the risk of financial losses for the parties involved. The effectiveness of fraud rules in Vietnam depends on the level of awareness and compliance among all stakeholders, including banks, exporters, importers,

and government agencies, as well as the availability and accessibility of relevant information and resources.

The adoption and implementation of international best practices for fraud prevention and detection in Vietnam can increase the trust and confidence of foreign partners and investors in the Vietnamese market, leading to more opportunities for trade and investment and greater access to global resources and networks. The alignment of fraud rules with international norms and guidelines can improve the transparency and predictability of the legal and regulatory environment in Vietnam, promoting a culture of compliance and ethical behaviour and reducing the risk of reputational damage and legal liabilities for Vietnamese businesses.

These hypotheses will likely be further explored and tested through legal research, analysis of case law, and interviews with industry experts, in order to determine their feasibility, efficacy and potential impact on protecting Vietnamese merchants from fraudulent activities in letters of credit.

f. Research methods

The methods used in this study are:

- Doctrinal study research: This approach is used to explain the philosophy and legal concerns surrounding letters of credit, the regulations, the specifications for the provided papers, etc. The theories and legal requirements will be examined, and the findings will be used to analyse the case study and provide remedies.
- Historical research: This approach is employed to assess the efficacy of fraud rules and legal restrictions over time. As a result, the author will have a basis for evaluating the existing circumstances and legislative framework in Vietnam, and as a result, the remedies may be demonstrated in this research.
- The comparative research: Following a judgment of the shortcomings in the Vietnam regulations, the author will inherit and apply the improvement to the current dearth of regulations in the Vietnamese legal system. This method is used to explain the benefits and drawbacks between national laws and international regulations regarding the law of the letter of credit and fraud rules. The laws of the United States, which reflect common law, and those of the People's Republic of China, which are comparable to the legal system in Vietnam, will be used in this study. To get a bigger picture, the international regulations are also looked at.
- The qualitative research: The author shall recommend for the effective resolutions to protect the honest party in the letter of credit by issuing fraud rules from her perspective. The author uses the numbers and charts through surveys and publications from the Vietnam Government regarding the development using the letter of credit in the financial industry as well as the announced defraud numbers to evaluate the effectiveness of the current regulations in letters of credit law.

g. Framework

The framework of my dissertation will be divided into 10 chapters.

Chapter I will introduce the history of letters of credit. The commercial background of letters of credit will be investigated and the brief history of the letter of credit will be carefully considered to give a whole view of this instrument.

Chapter II shows the sources of the letter of credit law. The Uniform Customs and Practice for Documentary Credits published by the International Chamber of Commerce is considered the essential source of law for letters of credit since it has a specified influence on international regulations. Hence, besides the discussion about the drafting and revision of the Uniform Customs and Practice for Documentary Credits, I will introduce and discuss the other relevant subject areas such as the Uniform Customs and Practice for Documentary Credits for Electronic Presentation and the International Practice Standby, etc. The provisions of the United Nations Convention on Independent Guarantees and Standby Letters of Credit will also be mentioned. Case law also provides a prominent part of fraud rules in the letter of credit law, hence, the precedents and court decisions from different jurisdictions will be given in this thesis.

Besides the commercial letter of credit that will be discussed in this thesis, **Chapter III** will briefly mention the nature of letters of credit, different stereotypes of letters of credit as well as their commercial utility.

The relations between parties will be analysed in **Chapter IV** to clarify the operations of the letter of credit as well as the parties' obligations and rights. **Chapter V** will give specific information about the documents followed by the credits.

Chapter VI will describe both principles which are considered the backbones of the letter of credit: the Independent principle and the Strict Compliance principle. The centre of the documentary credit law is the Independence principle. According to this principle, the issuing bank must pay for the documents tendered by the beneficiary, this commitment is separated and ultimately independent from the sales contract between the seller and the buyer and the reimbursement contract between the bank issuer and the applicant.

Even though the Uniform Customs and Practice for Documentary Credit is applied in most international letters of credit, it still leaves some problems for domestic law, one of which is the fraud exception. **Chapter VII** shall mention a few countries that tried to have fraud rules such as the United States of America and the People's Republic of China. This Chapter also focuses on the "fraud exception" in international regulations, the Uniform Customs and Practice for Documentary Credit *and* the United Nations Convention on Independent Guarantees and Standby Letters of Credit.

In the last chapter, **Chapter VIII**, the author will evaluate the letter of credit law in the Vietnam Legal System. Since the courts and merchants in Vietnam can consult the Uniform Customs

and Practice for Documentary Credit rules about definitions of the letter of credit and obligations of parties, etc, however, relying entirely on the UCP is not a good idea because the Uniform Customs and Practice for Documentary Credit is not complete in dealing with fraudulent activities. The author then will try to propose a resolution from her perspective on the legal interpretation of the letter of credit and fraud rules in **Chapter IX** and give conclusion remarks on **Chapter X**.

CHAPTER I

THE HISTORICAL REVOLUTION OF LETTERS OF CREDIT

Letters of credit are known for a few centuries[1] (Trimble, 1948, p. 981) (Miller, 1959, pp. 162-166). In their original form, letters of credit involved two parties in which a wealthy party promised to pay the other party an amount of money through a letter. In exchange, the other party would ship the goods to the agent of the aforesaid wealthy party (Miller, 1959, pp. 162-163). Merchants at that time used letters of credit among themselves and letters of credit were supported through the networks of merchants (Malynes, 1622) (Miller, 1959, p. 163).

Some experts assume that letters of credit originated in ancient Egypt and Babylon; Trimble has mentioned a clay note from Babylon which is expected to date from 3000 B.C. This clay note promised to pay back an amount of money on a stipulated date (Trimble, 1948, p. 982). Another reference is an obligation which is made in 248 B.C. from Egypt for repayment (Wigmore, 1936, p. 69). After the collapse of the Roman Empire, it took centuries and was not until the late 12th century and early 13th century for banks in European cities to re-establish. Then the merchants faced some trading issues such as the dangers to travel with gold or the currency generated by commerce did not satisfy the needs of traders, etc. Letters of credit are issued to solve such problems by the merchants[2].

It is acknowledged that the first form of letters of credit is the bill of exchange appeared in the early Mediterranean in the twelfth century. With some historians, it would be called the letter of payment (Usher, 1943) (Kozolchyk, 1965, p. 395). There were four parties in the ancient letter of payment which are “the remitter, the maker or drawer, the payor and the payee” (Usher, 1943) (Kozolchyk, 1965, p. 395). However, it was not clear whether the result of cambium (the contract of exchange) was the letter of payment or it was a combination of an extension of credit and the contract of exchange (Goldschmidt, 1891) (Kozolchyk, 1965, p. 396). A characteristic that was usually left out of both the letters of exchange and the letters of payment was these letters did not include a specific pledge to pay but a simple order of payment: “It was not until a series of consultations were given by the fourteenth-century post glossators that the assimilation of the order of payment with the informal promise of payment took place.” (Usher, 1943, pp. 88-89) (Kozolchyk, 1965, p. 396).

Some scholars contend that their development in Europe was inspired by Marco Polo's 13th century discoveries, which reported how to use currency and other transferable documents in China, confirming that this kind of indicator formed one of the factors for “the ways and means by which the Great Chan can have and indeed does have more treasures than all the kings in the world” (Davidson, 1995, p. 129).

[1] Some opinions show that the letter of credit was used since the twelfth century.
[2] Merchant also created bills of exchange (or draft).

Later, in the seventeenth century, on the European continent and in England, the bill of exchange started to be considered a negotiable instrument and it was usually found as "letters of credit" and was defined as "a merchant doth send his friend or servant… to buy some commodities or take up money for some purpose, and doth deliver unto him an open letter directed to another merchant requiring him that his friend, the bearer of that letter have occasion to buy commodities or take up money… that he will procure him the same and will provide him the money or pay him by the exchange." (Malynes, 1622, p. 104).

Since business grew in scale, along with the size of international transactions, the network of merchants was not sufficient to guarantee the credit of an individual buyer (Leon, 1986, p. 433). Hence, merchants needed an independent party – normally a bank – to secure the payment between the seller and their unknown or remote buyer (Leon, 1986, p. 433). Accordingly, a third party was adjoined to modern letters of credit. The essential function of letters of credit stayed the same: to provide a guaranteed mechanism for payment associated with a sales transaction (Leon, 1986, p. 433).

Compared to its previous form, the letters of payment, in the twelfth century, letters of credit required multiple parties and several transactions. For example, the Ordenanzas de Bilbao of the Spanish in 1737 had declared the Cartas Ordenes de Credito (translated as "letters of credit"). This Code also provided the legal scheme for the adoption of letters of credit in the commercial codes in Spain and Latin- America (Kozolchyk, 1965, p. 397).

The most noticeable characteristics of the Cartas Ordenes de Credito were (i) letters of credit will only be issued concerning "*tomador, portador or preneur"* (a designed person) and the given payee will never be given the "order of"; (ii) a certain amount of payment must be included in the instrument. Letters of credit would not be considered merely the letter of recommendation if they lacked these two requirements (Kozolchyk, 1965, p. 397).

The Cartas Ordenes de Credito in the nineteenth century was not a perfect instrument for purchasing foreign products since the financier or the seller or his beneficiary could comfortably turn to this instrument as a guarantee to assure the payment and the duties of the parties. Instead, this instrument was limited to a financial device between multiple merchants that usually believed in credits or open accounts. This model of letter of credit is called "buyer's credit" in the United States, and it was famously used in domestic transactions in the middle of the nineteenth century in Europe and Latin America (Finkelstein, 1931, p. 497) (McCurdy, 1922) (Thayer, 1936, p. 1033).

Letters of credit arose in the United States as a result of competition among factoring companies for business, which resulted in the issue of guarantees to take drafts in the shipping (Kozolchyk, 1965, pp. 395-398). The increased use of letters of credit was enabled by the expanding manufacturing companies and their links with international traders, the specialisation of banking operations, and advancements in technology including the increased utilization of telegraph for transmitting contractual requirements (Kozolchyk, 1965, pp. 395-398).

Letters of credit, on the other hand, were not just utilized by traders (Tóth, 2006, p. 3). In 1803 while commanding an endeavour to survey the untamed western nation, Thomas Jefferson, the third president of the USA, sent a message to Captain Meriwether Lewis stating Captain Meriwether Lewis might find himself without money, clothing, and other requirements because a significant quantity could not be brought with him from the US. In that case, his sole resource is the credit of the United States, hence, Captain Meriwether Lewis might be able to find the letter of general credit negotiable for obtaining money or necessaries (Tóth, 2006, p. 3).

The advent of World War I shattered the long-established and trustworthy commercial relationships that had formed between businessmen across the world. Merchants were obliged to form new relationships with businesses that were frequently unidentified or untrustworthy in order to continue dealing. These conditions were favourable for the widespread use of letters of credit, which brought a reliable financier, a bank, into the traders' connection. By the 1950s, letters of credit had established a leading position in US domestic economies and were frequently employed in foreign transactions. Since World War II, the usage of letters of credit in international trade has been consistent. Although the introduction of other forms of trade financing occasionally outshines the usage of the letter of credit, it has shown to be a flexible instrument that can be easily adapted to the demands (Tóth, 2006, p. 3).

CHAPTER II

THE LAW OF THE LETTER OF CREDIT

2.1. The Uniform of Customs and Practice for Documentary Credits

2.1.1. The Birth of UCP

Letters of credit are believed to gain their popularity since the First World War ended (Ellinger, E.P., 1970, p. 106). Before that time, the usage of letters of credit was not common (Dolan, 2001, p. 4). Ever since then, the uniformity of the letter of credit practice was urgently required to be formed. Professor Ellinger explained the reason why the usage of documentary credits became increasingly high in the post-war is because of the lack of economic stability (Ellinger, E.P., 1970). The security for the transactions became important since the merchants flourished or went bankrupt in simply one night (Dolan, 2001, p. 4). The merchants also saw themselves trading with oversea partners whom they knew little about, living beyond the sea and having no guarantees in the economy and political situations.

Hence the obligation in alternate finance of letters of credit is to contribute the security to the parties and this obligation is considered the primary task of the documentary credits (Dolan, 2001, p. 3). The New American Commercial Credit Conference in 1920 attempted to form uniformity for the regulations of the letter of credit. In Europe, many countries also sought standards and rules for this type of mechanism (Dolan, 2001, p. 37). In 1923, Germany (Schütze & Fontane, 2001, p. 120) and Greece followed the US's path, then 1924 was France and Norway's turn. Czech, Slovakia, Italy, and Sweden did their own set of regulations in 1925. Argentine has its own rules in 1926 and the Netherlands followed in 1930 (E.P.Ellinger, 1982, p. 248).

However, the Uniform of Commercial Practice for Documentary Credits (hereinafter referred to as "UCP") issued by the International Chamber of Commerce (hereinafter referred to as "ICC") is the most essential guideline for the law and the practice relating to the letter of credit. M. Kurkela said "there could hardly be anything more international in the field of law than the letter of credit" (Kurkela, 1972, p. 9). This statement has reflected the reality that the UCP has unified the universal practices in the banking industry associated with letters of credit. Technically, nearly all the banks in all countries use these regulations to govern their letters of credit reflecting its popularity.

2.1.2. The History of UCP

The ICC first attempted to standardize the international practice of letters of credit in its congress in 1929. Unsuccessfully, only banks in Belgium and France accepted the proposed unified law. The UCP then went through a revision and was adopted in 1933 again with shortened name UCP 82 (International Chamber of Commercial, 1933). This UCP version was

adopted by some bankers in the finance industry but not in the United Kingdom and the Commonwealth Countries (Ellinger, 1984, p. 578).

After the break from World War II, the next revision of UCP was adopted at the Lisbon Conference in 1951 (International Chamber of Commerce, 1951). As Henry Harfield said that "[T]he purpose … is to codify the custom and practice as they now exist." (Harfield, 1979, p. 4). This 1951 version was accepted widely but again not by the United Kingdom and the Commonwealth Countries.

It is not until the version of UCP 1962 (International Chamber of Commerce, 1962) that bankers in the United Kingdom and the Commonwealth countries accepted to use. Professor Ellinger considered the adoption from the United Kingdom very important and the UCP 1962 had made it (Ellinger, 1984, p. 580). Because of the development in technologies, the UCP needed a revision in 1974[3] (International Chamber of Commerce, 1974) and it was revised again in 1983 (International Chamber of Commerce, 1984). With the UCP 1983 (International Chamber of Commerce, 1984), the ICC added a new type of letter of credit which was the standby letter of credit into the scope of UCP. This version focused on different issues such as the negotiation of the document of documentary credit, the adoption of the new type of letter of credit, and the new technologies used in the transmission like SWIFT- Society for Worldwide Interbank Financial Telecommunications (Ellinger, 1984, p. 582). In this version, UCP started to apply for both standby letters of credit and commercial letters of credit.

Afterwards, the ICC has revised UCP again in 1993 to improve its function because nearly fifty per cent of the tendered documents were turned down by the banks because of the discrepancies (International Chamber of Commerce, 1993), and the ICC also wanted to "address new developments in the transport industry and new technological applications (International Chamber of Commercial, 1933). This ratio highlighted the imperfect operation of the UCP and caused losses to the merchants in international trade. Hence, the new version is adopted and recognized as ICC Publication No. 500 or UCP 500.

The latest version is UCP 600 and is valid on 01 July 2007. UCP 600 has 39 articles and applies to "bankers, lawyers, importers, and exporters, transport executives, educators, and everyone involved in letter of credit transactions worldwide" (International Chamber of Commerce, 2007). Nowadays, most letter of credit is governed by UCP (Xiang & Buckley, 2003, p. 112) and most bankers and merchants use UCP although the UCP is not law.

It is irrefutable that the uniformity in the international procedure of letters of credit is mainly contributed by the UCP and it also presents explanations for the banks using this kind of payment mechanism. However, it should be noted that the practice in this area will never be completely united since there are different understandings and several practices in each country around the world (Hofstede, 1994, pp. 1-2). As Professor Ellinger had stated, the legitimate

[3] 162 countries and territories had accepted the revised version in 1974. Such information is recorded in ICC Document No. 470/383 of June 1,1981.

intention of letters of credit was to substitute finance for the international transactions (Ellinger, E.P., 1970, p. 2), and to have some uniformity for the operation of letters of credit.

2.1.3. The Nature and Application of the UCP

The UCP is considered "the most successful harmonizing measure in the history of international commerce" (Gao, 2002, p. 18). Even though the UCP defines the liability and responsibility of parties in letters of credit and is widely accepted in many countries in the world, it is still not considered law since it does not have legislative authority. Lord Mustill in *Royal Bank of Scotland Plc v. Cassa di Risparmio delle Provincie Lombarde* stated that the UCP's terms "do not constitute a statutory code" because the UCP had precisely expressed that they only had "a formulation of customs and practice" (Royal Bank of Scotland Plc v. Cassa Di Risparmio Delle Provincie Lombard and Others, 1991). His Lord continued to impress that the parties could cooperate with the UCP in their letter of credit by stating that their letter of credit shall be governed by the UCP (Royal Bank of Scotland Plc v. Cassa Di Risparmio Delle Provincie Lombard and Others, 1991). According to Professor Ellinger, UCP should be considered a "de facto law" (Ellinger, 1984, p. 578). The rules of UCP are universally used in many courts because of the existing industrial practices reflected in its (Xiang & Buckley, 2003, p. 113).

The UCP has also stated that its application is only available when parties agree to apply it in their agreement:

> "The Uniform Customs and Practice for Documentary Credits, 2007 Revision, ICC Publication No. 600 ("UCP") are rules that apply to any documentary credit ("credit") (including to the extent to which they may be applicable, any standby letter of credit) when the text of the credit expressly indicates that it is subject to these rules. They are binding on all parties thereto unless expressly modified or excluded by the credit." (International Chamber of Commerce, 2007)

2.2. Supplement to the Uniform Customs and Practice for Documentary Credits for Electronic Presentation

The eUCP stands for Supplement to the Uniform Customs and Practice for Documentary Credits for Electronic Presentation. The eUCP is drafted to "formulate rules for the evolution from paper-based credit to electronic credit" (Byrne, et al., 2002).

The tasks in the future of ICC emphasized that UCP needed to adapt the new electronic technology applied in the letter of credit. So, on May 24, 2000, an ad hoc group was formed to formulate an addendum to the UCP. This addendum would handle the presentation stages where the documents are submitted in electronic form (International Chamber of Commerce, 2001). This supplement was accepted by the ICC Banking Commission in Frankfurt on November 07, 2001. eUCP Version 1.0 came into force on April 01, 2002. The latest version of eUCP is eUCP Version 2.0 which was issued in 2019 and is used to govern the electronic

presentations of the letter of credit shall be briefly mentioned in this thesis but will not be well addressed since, after the eUCP version 1.0 is issued, the percentage of the e-trade business still constitute less than 1% of the finance field (Godier, 2000). Electronic documents are not strongly believed to make a compelling profit until a few years later (Godier, 2000) (Katsman, 2002, pp. 16- 17) (Barnes & Byrne, 2001, p. 33).

The supplement eUCP support a lot of issues for UCP such as the "format, presentation, originals and copies, and examination of electronic records." (Xiang & Buckley, 2003, p. 114). To embody the eUCP within the letter of credit, parties must specify to apply the eUCP in the letter: "All articles of the eUCP are consistent with the UCP except as they related specifically to electronic presentations." (International Chamber of Commerce, 2001). According to the regulation in UCP, the subject of eUCP is the subject in the UCP without meeting any difficulties.

2.3. International Standard Banking Practice

The "international standard banking practice" was first mentioned in Article 13(a) of UCP 500 and now it is implied in Article 2 of UCP 600. At first, there was no definition for what comprised "international standard banking practice" (Busto, 1993, p. 39). The New York Bankers Commercial Credit Conference had given its first attempt to standardize the banking practice by issuing a checklist in 1920. The list was called "Regulations affecting Export Commercial Credits". Then the International Financial Services Association (which back then was called "The US Council on International Banking") issued a paper named "Standard Banking Practice for the Examination of Letter of Credit Documents" which provided a list of activities that banks should consider while checking the presented documents. However, this checklist was only reflecting the perspective of the IFSA member banks (Smith, 2000).

The urge to have well-detailed instructions on the definition of "international standard banking practice", a Task Force was formed in 2000 by the UCC Banking Commission. As has been stated, more than 50% of presented documents were rejected due to discrepancies[4] (Meynell, 1998) (Shaw, 1999), hence, it was an assignment of the Task Force to gather and recorded the universal banking practice to renew the rules (International Chamber of Commerce, 2002). After several months of collecting and checking enormous practices in the banking industry worldwide, the Task Force submitted the International Standard Banking Practice for the Examination of Documents under Documentary Letters of Credit (hereinafter referred to as "ISBP") (International Chamber of Commerce, 2002).

The ISPB was expected to "evolve[d] into a necessary companion to the UCP for determining compliance of documents with the terms of letters of credit." and "by using the ISBP, document checkers can bring their practices in line with those followed by their colleagues worldwide" (International Chamber of Commerce, 2002). However, the ISBP does not alter the UCP.

[4] The UCP 500 opening has stated that there are numbers which show that around 60-70% of the documents are rejected in the presentation stages because of discrepancies.

The ISBP continued to apply during the time UCP 600 is in force (International Chamber of Commerce, 2007). The banking industry welcomes the ISBP due to some belief that ISBP helps the users in the banking practice (DC Insight, 2003). The ISBP was updated in 2007 under the name of PCC Publication No. 681 and was revised in April 2013 under the name ICC Publication No. 745. This revision was considered to have a better connection with the UCP 600 and followed the set-up of the UCP 600 for better reading.[5]

2.4. International Standby Practice

The International Standby Practice (hereinafter referred to as "ISP 98") is specially designed for standby letters of credit[6] since banks in the United States are banned from using guarantees. It could be understood that the standby letters of credit are the substitute for the guarantees. The standby letters of credit have gained a reputation over several years, however, there were no regulations to govern them. The subject of the standby letter of credit is mentioned in the UCP since UCP 500 (International Chamber of Commerce, 1993), however, the UCP is originally written for commercial letters of credit so some provisions could not be practised with standby letters of credit (P.S. Turner, 1999, pp. 457-459).

ICC has issued some regulations to govern the standby letters of credit such as URDG, however, "from the viewpoint of the ICC, […] standby letters of credit continue to be covered by the UCP and are not covered by the URDG." (P.S. Turner, 1996, pp. 205-207) (Byrne, 1997) (Affaki, 1999). Then, ISP 98 was created by the United States-based Institute for International Banking Law and Practice, Inc. with the support of the US Council on International Banking. ISP 98 was adopted in 1998 by ICC (Institute of International Banking Law & Practice, 1998) and came into force in January 1999. According to Professor Byrne, "its reception has been, on the whole, very positive." (Byrne, 1999, p. 180).

As has been seen, ISP98 was originally designed only for standby letters of credit just like the UCP was originally formulated for commercial ones. The ISP 98 helps lawyers and judges with the interpretations of the practice of the standby letters of credit when some problems are not covered by domestic law. ISP98 not only applies to the standby letters of credit but also applies to "any independent undertaking issued subject to it" according to Article 1.01(b) of ISP98 (Institute of International Banking Law & Practice, 1998).

2.5. United Nations Convention on Independent Guarantees and Standby Letters of Credit

Under the view of ICC, UCP is not law, so the fraud exception is left as a national issue, which led to several problems because of differences in legal systems between countries or

[5] The latest version of ISBP 745 is up to date at: https://2go.iccwbo.org/international-standard-banking-practice-isbp-config+book_version-eBook/#details.

[6] The modern letter of credit has two kinds which are the commercial letters of credit and standby letters of credit. The term "letters of credit" in general shall has another name as "credit". Within this thesis, the commercial letters of credit shall be referred to as "documentary credit" or "commercial credit". The standby letters of credit shall be only referred to as "standby credits" or "standbys".

differences in standards of fraud, etc. On the contrary, the United Nations Convention on Independent Guarantees and Standby Letters of Credit (hereinafter referred to as "UNCITRAL Convention 1995") has tried to solve the problems that put difficulties in international transactions for a long time by concentrating on the rule of fraud and set a standard to define fraud to cover the honest users of standby letters of credit and independence guarantees[7].

The United Nations Convention on Independence Guarantees and Standby Letters of Credit was drafted by UNCITRAL in 1995, was valid on 01 January 2000, and was signed by United Nations General Assembly. This Convention is an attempt to regulate the international independence guarantees and international standby letters of credit (Davidson, 2010, p. 31), the parties nonetheless can apply this Convention to the commercial letters of credit if they clearly express their wishes to use the UNCITRAL Convention 1995 to regulate the commercial letters of credit in light of Article 1 of the UCNTRICAL Convention 1995 (UNCITRAL, 1995).

> "This Convention applies also to an international letter of credit not falling within Article 2 if it expressly states that it is subject to this Convention."

The application of this Convention to domestic letters of credit is strictly minimal. The difference between UCP and UNCITRAL Convention 1995 is the UCP is drafted by a private organization which is ICC, while the UNCITRAL Convention 1995 is considered a law for countries to adopt as stated in Article 1 of the UNCITRAL Convention 1995 (UNCITRAL, 1995). The remarkable points of the UNCITRAL Convention 1995 are the rule regarding fraud in the standby letters of credit as well as the independent guarantees and the judicial remedies for such problems (Xiang & Buckley, 2003, p. 117). As has been stated, the UNCITRAL Conventional 1995 is still applied to commercial letters of credit if parties wish to use the UNCITRAL Convention 1995 to regulate their commercial letters of credit (UNCITRAL, 1995).

However, the point of view of the UNCITRAL Convention 1995 about fraud was denounced by some legal scholars, for example, Professor John F. Dolan indicated that the UNCITRAL Convention 1995 had stumbled in defining and confronting fraud problems (Dolan, 1996, p. 63). The reason for this criticism was the approach of the UNCITRAL Convention 1995 to fraud. In the UNCITRAL Convention 1995, the word "fraud" is not directly introduced in Article 19 and Article 20 (UNCITRAL, 1995). The reason behind this, as Professor Bergsten mentioned in (1993, p. 859), was because the diversities in different domestic law systems might lead to chaos in clarification of fraud, so to avoid this problem, UNCITRAL Convention 1995 tried not to use the word "fraud" in its terms.

2.6. Uniform Commercial Code of the United States

[7] The UNCITRAL is established in 1966 by the General Assembly. The UNCITRAL is an intergovernmental body working on the progressing harmonization of the international trade law. See more information regarding the UNCITRAL at http://uncitral.org/uncitral/en/about_us.html.

The United States (hereinafter referred to as "US") is one of the independent countries having an article to regulate the process of letters of credit. The law of letter of credit is embedded in Article 5 of the Uniform Commercial Code (hereinafter referred to as "UCC"). The UCC is not federal law but is considered a uniformly adopted state law, hence there will be different versions of Article 5 of UCC in different states.

The National Conference of Commissioners on Uniform State Law[8] was founded in 1892 due to the suggestion of the American Bar Association. Since its beginning, there are more than 200 uniform laws drafted by the Conference. Among these laws, commercial law is considered the most compelling success (White & Summers, 2000, p. 3). By the year 1930-1940, due to the growth in "large scale commercial law reform" (White & Summers, 2000, p. 3), William A. Schnader proposed to modernize and replaced the previous commercial uniform act. Then the Uniform Commercial Code is first published in 1952 with 11 articles. Pennsylvania is the first state to adopt the UCC in 1953 and in 1968, 49 states of the US had accepted the Code. The UCC covered nearly the whole commercial law and had "Official Comments" in every section.

The first version of Article 5 in the UCC 1952 was not considered a "code" compared to other articles in UCC, it was drafted to create a theoretical framework that was independent and could flourish later in the future. Due to some scholars, the fraud rule in Section 5-114(2) was considered a "basis for future development" (Buckley & Gao, 2002, p. 684), however, it was not entirely faultless and remained several problems. Besides the lack of fraud standards, the confusion also lies in where fraud should be located, and whether fraud should only be examined in the documents or should be extended to fraud in the underlying transaction (Buckley & Gao, 2002, p. 684). These problems led to the reduction of the commercial utility of letters of credit in the international trade (Flint, 2019, p. 384). In 1995, Article 5 is revised due to "weaknesses, gaps, and errors in the original statute which compromise its relevance" (Task Force, 1990, p. 1532). The development of technologies in letter-of-credit transactions is also a reason to revise Article 5.

The revised version of Article 5 is presented in October 1995 and fraud rules are now defined in Section 5-109 (Uniform of Commercial Code, 1995). According to this version, the main obligation of bank issuers is to honour the presented documents from the presenter on condition that such documents satisfy the requirements in the letter of credit. This obligation cannot be cancelled based on the applicant's accusation stating that the beneficiary does not fulfil their obligations in the underlying contract. Issuing banks must pay for the documents tendered by the beneficiary if the documents comply with the requirements in the letter of credit. If there are any problems raised from the underlying contract related to the obligations of the seller, the buyer could recover his loss in a suit for breach of warranty (Flint, 2019, p. 372).

[8] For further information about NCCUSL, visit http://nccusl.org.

Even though Article 5 was completed and adopted in the United States, however, UCP still plays an important role in the financial transactions happening in the US. Most of the transactions using letters of credit are still governed by the UCP and so, “the UCP will be a more significant source of law than the UCC.” (White & Summers, 2000). Article 5 might have some rules in common with the UCP, however, it remains an official article in a code. Article 5 mainly governs the liabilities and responsibility, fraud rules, and international banking lawyers can inform themselves about the mechanic of letters of credit through rules provided by UCP.

CHAPTER III

THE NATURE OF LETTERS OF CREDIT

3.1. What is a Letter of Credit?

Letters of credit are defined under Article 2 of UCP 600 as follows:

> "Credit means any arrangement, however, named or described, that is irrevocable and thereby constitutes a definite undertaking of the issuing bank to honor a complying presentation."

Within the definition, the letter of credit is interpreted as an irrevocable mechanism, in which the issuer commits to set up a settlement against the submission of the documents on their face to comply with the requirement of letters of credit. Professor Ellinger concluded that the modern letter of credit took its form around the year 1840 and became "respectable" about the year 1849 (Ellinger, E.P., 1970, p. 29), which in the middle of the 19th century and thoroughly perfected after the First World War (Ellinger, E.P., 1970, p. 37).

The modern letter of credit can be divided into two forms: standby letters of credit and commercial letters of credit (Richard F. Dole, 2008, pp. 735-739). Commercial letters of credit are considered the classic form of letters of credit (Xiang & Buckley, 2003, p. 95) and are used as an instrument to pay the seller in the international transaction on which the letter of credit is based (Flint, 2019, p. 359). In common law countries, commercial letters of credit are often called "documentary credit" or "bankers' commercial credits". Standby letters of credit conduct the legal framework which is similar to a commercial letter of credit. Standby letters of credit are normally adopted by a considerable range of transactions, and it is usually used in the construction industry, financial industry, or in the sale contract of goods to guarantee the performance of the good purchased (Xiang & Buckley, 2003, p. 99).

3.1.1. Commercial Letters of Credit

A letter of credit is a creation of international commerce and serves as a financing mechanism for merchants. Commercial letters of credit are usually used to assure the parties' fears, which are mainly payment problems and the quality of the goods, in international transactions (Gao, 2002, p. 3). For instance, assuming a merchant in the United States wants to buy goods from a Vietnamese seller, however, both merchants do not have any relationships before and know nothing about each other. The seller is afraid that if he invests in producing and sending the goods oversea, the buyer might become insolvent or even worse, disappear after receiving the goods without paying. Once the situation happens, it incurs a large expense on the seller to arrange the goods or ship them back to the seller's place. The seller may lose money if he tries to resell the goods in the United States at a below-contract price. If the buyer rejects to pay for the goods they have received, the seller will take legal action and requires litigation in a foreign court which is belonged to a different legal system. The seller is at a disadvantage position compared with the buyer's position because he is not familiar with the United States'

jurisdiction. In a different circumstance, the buyer also has doubts about the seller's reputation and has no reason to believe the seller will send the goods with conditions as agreed in the sales agreement if the buyer pays before receiving them. There might be a chance that the seller shall disappear if he receives money and then sends nothing. Hence, once the problems such as fluctuation of currencies, long distances or different jurisdictions happen, merchants tend to lean on legal instruments which reduce the risks of parties in international trade.

To meet each other requirements relating to payment and sending/receiving goods, merchants and banks have come to a solution to use a financial instrument issued by banks. Parties use the letter of credit as a mechanism to minimize the risks and include the protection for their sales contract (Leacock, 1984, p. 886). Commercial letters of credit ensure the buyer that goods conformed to the requirements in the sales contract will be shipped before the seller receives the payment and provide the seller with an assurance that payment is approaching. By this mechanism, the time when the buyer controls the goods is overlapped with the time the seller has their money (Megrah, 1982, pp. 255-256). Under the agreement between parties, the buyer shall instruct their bank to issue a documentary credit for the beneficiary (the seller). The bank shall examine the trustworthiness of the buyer and accepts his application. The bank then issues a letter of credit describing the basic requirements, including instructions and independence obligations of the bank to accept the documents submitted once they satisfy the demands illustrated in the letter of credit (Gao, 2002, p. 3). The presented documents normally include a commercial invoice describing the goods, a clean onboard bill of lading proving the goods are loaded on the vessel and is being sent to the buyer, and insurance; these papers are necessary to demonstrate the possession of the goods (Xiang & Buckley, 2003, p. 96).

3.1.2. Standby Letters of Credit

Standby letters of credit first appeared in the United States in the 1950s by American banks because the American jurisprudence had eliminated the usage of the banks' guarantees (Ellinger, 1978, p. 604). The standbys started to gain their reputation in international transactions in the 1970s (Buckley, 1996, p. 217) and the banks used them as a substitute for guarantees. The standbys are normally used to give the beneficiary protection if the other party does not carry out their obligations in the underlying contract.

Commercial letters of credit and standby letters of credit share the same characteristic in their legal nature, however, there are some differences between these two kinds of credit:

First, each kind of letter of credit has its economic functions. While the commercial letter of credit is a tool to ensure that the seller will be paid if he presents the complied documents; the standby letter of credit is created as a guarantee to assure the beneficiary that the applicant will fulfil his duties in the underlying contract, otherwise the beneficiary will receive reimbursement for non-performance or imperfect implementation of the applicant. Normally, the beneficiary in the standbys does not expect to be paid while the beneficiary in the commercial letters of credit has the opposite wishes (Xiang & Buckley, 2003, p. 100).

Second, the documents tendered by the beneficiary in the commercial credit are different from the ones in the standby. Presented documents in the commercial credit shall prove that the seller has accomplished his duties in the underlying contract (McLaughin, 1986, p. 40). In the standby, the documents needed to be presented to the bank are either a "sigh draft" or "a demand for payment" and a signed document proving that the applicant does not fully accomplish his duties in the underlying contract (Flint, 2019, p. 364).

Third, a standby letter of credit faces more risks than a commercial letter of credit. The commercial letter of credit requires a set of documents including a bill of lading (a clean on-board bill of lading is needed under the UCP 600), an invoice, and other papers to demonstrate that the beneficiary has accomplished his duties, which give the applicant and the issuing bank a high level of security (Xiang & Buckley, 2003, p. 100). Meanwhile, the beneficiary in the standby is only required to present a sight draft or sometimes a demand to pay to the issuer. Sometimes the bank issuer requires certificates from third parties, but this does not reduce the risks in the standby. Therefore, "the potential for sharp practice and outright fraud is far greater in most cases in the use of standby credits than it is with trade-related credits" (Buckley, 1996, p. 228).

Despite such disadvantages, the range of applications for standby letters of credit is wider than commercial letters of credit. While the commercial one could only be used in a sales transaction, the standby letter of credit has no limitation in the application. The contracts which can apply the standby letters of credit vary if there is one party's performance is executory (Davidson, 2010, pp. 1-24). There are some fields where the standby letter of credit is used more than others such as the construction industry where the owner is protected from slow conduct or non-performance of the contractor, or in international sales, transactions to ensure the performance of the machine or equipment bought (American Bell Intern. v. Islamic Republic of Iran, 1979) (Joseph, 1977, p. 126).

3.2. Types of letters of credits

3.2.1. Sigh payment, deferred payment, acceptance, or negotiation

Parties must have a meeting of the minds on what type of credits they want to use, and the letter of credit must be issued accordingly. Under Article 6 of the UCP 600, it must be stated whether the credit is "available by sight payment, deferred payment, acceptance or negotiation" (International Chamber of Commerce, 2007).

a. Sight payment: payment against documents. Once the beneficiary presents the documents complying with the requirements under the credit, the bank shall honour it after a specific checking period. According to Article 14(b) of UCP 600, the investigation shall be carried on in five banking days (International Chamber of Commerce, 2007);
b. Deferred payment: payment will be fulfilled at its deadline. A deferred payment credit means that the presenter will be paid at a decided date stated in the credit. For instance,

the credit will provide a 90-day payment after the date of shipment or a 30-day payment after the presentation. Once the tendered documents conform to the requirements in the credit, the bank will give the beneficiary a statement stating the settlement will be fulfilled on the maturity date.

c. Acceptance credit: the issuer is obligated to accept the drafts drawn by the beneficiary and pay on the maturity day. In case the drafts are refused by the nominated bank, the issuing bank shall entitle to pay for the beneficiary as stated in Article 2 of UCP 600 (International Chamber of Commerce, 2007) (E.P.Ellinger, 1982, p. 246).
d. Negotiation credit: the negotiation credit is defined under Article 2 of UCP 600 as "the purchase by the nominated bank of drafts (drawn on a bank other than the nominated bank) and/or documents under a complying presentation, by advancing or agreeing to advance funds to the beneficiary on or before the banking day on which reimbursement is due to the nominated bank" (International Chamber of Commerce, 2007). The negotiating bank shall "purchase" the drafts or documents with an amount of deduction of interest. There are certain limited banks named negotiating banks (International Chamber of Commerce, 2007). Furthermore, it is necessary to recognize that the documents under letters of credit might be negotiated, not letters of credit. Letters of credit themselves are not negotiable.

3.2.2. Revocable and Irrevocable Credits

Under the light of Article 3 of UCP 600, "a credit is irrevocable" when there is no expression about that (International Chamber of Commerce, 2007). And in Article 2 of UCP 600, irrevocable credit is "a definite undertaking of the issuing bank to honour a complying presentation" (International Chamber of Commerce, 2007) which means the irrevocable credit shall not be adjusted or cancelled if the beneficiary does not give his consent; hence, the irrevocable credit gives the beneficiary a greater guaranty.

On the other hand, the revocable credit means it could be revised or cancelled without notice to the beneficiary. Thus, the consent of the beneficiary is not necessary (Busto, 1994, p. 36). Hence, this kind of credit does not give the beneficiary the assurance he wants.

In Article 6 of UCP 500, the issuing bank is required to affirm whether the credit is irrevocable. Without such implication, the credit is assumed as an irrevocable one (International Chamber of Commerce, 2007) (Busto, 1993, p. 14). In the latest version, Article 3 of the UCP 600, the credit is irrevocable except it states a different (International Chamber of Commerce, 2007).

3.2.3. Confirmed and Unconfirmed Credits

In the transactions of the credit, there might be other banks than issuing banks involved in the letter-of-credit transactions to perform as advising banks or confirming banks. The feature "confirmed" or "unconfirmed" of the credit relates to the attempts of these banks in the credit transactions.

- Confirmed credits

During the progress of letters of credit, another bank could be authorized to be a confirming bank by the issuer. The undertaking of the confirming bank is to confirm credit and states its confirmation undertaking toward the beneficiary. These undertakings might include accepting the draft, honouring, or negotiating considering Article 8 of the UCP 600 (International Chamber of Commerce, 2007). The confirming bank's duties are only triggered once the beneficiary presents the complied documents on time. The credit which is confirmed and irrevocable "give the beneficiary a double assurance of payment, since it represents both the undertaking of the issuing bank and the undertaking of the confirming bank." (Busto, 1994, p. 44). The confirmed credit normally includes text such as "… we hereby add our confirmation to the Credit in accordance with the stipulations under UCP…" (Busto, 1994, p. 42).

- Unconfirmed credits

In some circumstances, an advising bank is needed more than a confirming bank. The advising bank performs as an agency designed by the issuing bank, it is not required to confirm, "honor" or "negotiate" letters of credit as declared in Article 9(a) of the UCP 600 (International Chamber of Commerce, 2007), it must exam the trustworthiness of the credit. Hence, the letter of credit in this situation is considered unconfirmed.

The letter of credit which is unconfirmed usually contains this sentence: "This notification and the enclosed advised are sent to you without any engagement on our part" (Busto, 1994, p. 41). Even though the unconfirmed letters of credit are cheaper than the other ones, they are considered not "localize the performance of the contract of sale in the seller country." (Schmitthoff, 2000, p. 196).

3.2.4. Red Clause Documentary Credits and Green Clause Documentary Credits

The Red Clause Documentary credit is issued due to the financial requirements of the beneficiary before shipping products and the willingness to pay off the buyer (Harfield, 1944, p. 902). The Red Clause credit is described as follows:

> "The Read Clause is a device which originated in the China trade, where the seller was most frequently an agent of the buyer […] Accordingly, opening banks began to practice of endorsing on their credits in red ink (hence the name) a clause authorizing the confirming or negotiating bank to pay the beneficiary against the drafts alone, coupled with his simple promise to provide the documents in the future." (Ward & Harfield, 1948, p. 133) (Harfield, 1944, pp. 902-903).

The special condition to pay for the beneficiary was originally written in red ink, hence, this type of credit has its name following this feature (Union Bank of India, n.d., p. 7). In this credit type, the confirming bank or negotiating bank will pay in advance before the beneficiary tenders their documents as required under the authorization of the applicant (Union Bank of

India, n.d., p. 7). It is worth noting that it does not mean that the beneficiary is paid in advance without any presentation of documents, instead, they must present some documents such as a receipt of the warehouse or the evidence proving the existence of the goods. The willingness to pay the buyer even before the shipment of the products is expressed through the Red Clause credit.

In practice, for example, the buyer may want to buy the fur from Vietnam from a fur trader, however, the trader might not have enough cash to fund his suppliers as he collects here and there. Hence, the buyer could pre-finance the transaction by authorizing the bank to pay the trader in advance. The bank shall fund a certain amount of money under the requirement of the buyer once the trader provides some decided-on condition documents (Harfield, 1944, p. 904). The shipping documents will be submitted to the bank when the products are sent and the seller can receive the rest of the amount (Busto, 1994, p. 49).

The Green Clause Documentary Credit allows the beneficiary to receive in advance before shipping, but the goods must be in the warehouse under the name of the nominated bank (Union Bank of India, n.d., p. 7). This type of credit is understood as “refinement” of the Red one (Jack, 1991, p. 30). The pre-paid is conducted once the warehouse receipt is presented.

CHAPTER IV

THE MECHANISM OF LETTERS OF CREDIT AND STAGES OF LETTERS OF CREDIT

4.1. The Outline of Letters of Credit

The transactions in a letter of credit are formed from three sophisticated agreements but they are detached from each other. The first agreement is called the underlying contract which is the transaction between the buyer and the seller. The commitment of the buyer to process the payment to the seller via a letter of credit is demonstrated through this contract. Then, the applicant demands their bank a letter of credit. This request is the agreement between the buyer (now called "the applicant") and their bank (now called "the issuing bank" or "the issuer"). Issuing the letter of credit is the last step. The seller now is informed that he is the beneficiary of the credit, and the issuing bank declares that it is going to set the settlement against the submission of the documents described in the terms of the credit once all conditions of the credit are met (International Chamber of Commerce, 2007). In case of the payment must be practised outside the issuing bank's country, there will be the involvement of additional parties such as the confirmer, adviser, or negotiating bank.

Some critics are raised regarding the adoption of contract law into the letter of credit law to illustrate the relationships between parties and especially toward the relation of the issuer and the beneficiary (Xiang & Buckley, 2003, p. 92). The main reason for this objection is the absence of consideration in the letter of credit, however, the courts still constantly support the "validity and enforceability of irrevocable credits" and hold the opinion that there is a contract in the relationship between the issuer and the beneficiary (Ellinger, E.P., 1970).

In international trade, the sellers would not sell their products to the buyers unless they get a financial guaranty from well-reputation banks. Or else, the credit is used as an authentic agreement of the banks to substitute the financial strength or lending the reputation to buyers (Mann, 2000, p. 2525) (Dolan, 2001). According to Dolan, a letter of credit is "credit in nature" and is not governed by contract law (Dolan, 2001). It is governed by the letter of credit law and does not need consideration as stated under Article 5, Section 5-105 of the UCC (Uniform of Commercial Code, 1995). Trimble also supports this idea that "… the argument for regarding the irrevocable credit as a mercantile speciality is that the promise of the bank to the seller is binding because it is so considered by the business world and because it is couched in a form recognized by the customs of merchant…" (Trimble, 1948) (Ellinger, E.P., 1970, p. 106).

Due to the opening of the credit, the beneficiary shall carry out his duties and starts to collect the required documents. Once he submits the conforming documents, the bank will pay against these documents. Hence, the letter of credit is deemed to have a "go-ahead effect" (Kurkela, 1984, p. 25).

4.2. The Relationships between Parties

4.2.1. The Underlying Contract

Based on the underlying contract between the seller and buyer, the seller shall get his payment through a letter of credit. Therefore, the buyer must request his bank to issue a letter of credit in favour of the seller. In other words, the seller is obliged to get his settlement from the bank and is not allowed to demand the payment directly from the buyer when the letter of credit has not expired yet. Due to the independent principle in Article 4 of UCP 600, disputes that happened in this contract shall not affect the process of letters of credit (International Chamber of Commerce, 2007). Hence, the seller is allowed to directly request the payment from the buyer only when the letter of credit expires.

4.2.2. The Relationship between the Buyer (Applicant) and the Issuing Bank

In the contract for sales, the buyer (now known as the "applicant") must require their bank (now known as the "issuing bank" or "issuer") to issue a letter of credit in favour of the seller (now known as the "beneficiary"). The buyer will give their bank clear instructions in the application, he will list the documents which are needed to have possession of the products and other requirements which will affect the payment of the bank.

The bank shall enter the contractual relation once it accepts the application from the buyer. By entering this contract, the bank agrees to provide the payment for the beneficiary once he tenders the needed documents complying with the requirements of the letter of credit. These duties of the bank must be fulfilled to its best ability and in good faith. Consequently, the bank will get its reimbursement from the applicant right after it pays the beneficiary. The bank usually asks their customers to deposit an amount of money in the customers' accounts in the bank before opening the letter of credit. Later, the bank will directly charge the paid amount under the credit, the commission fee as well as other additional charges after honouring the credit from the buyer's accounts. Under the independent principle, this contract is separate from the underlying contract, and "the bank must strictly adhere to the buyer's instruction as set out in the application form." (E.P.Ellinger, 1982, p. 255).

4.2.3. The Relationship between the Seller (Beneficiary) and the Bank

By accepting the application of the buyer and issuing a letter of credit, the bank is engaged with its absolute undertaking to pay against the documents presented by the beneficiary complying with the requests of the credit[9]. The legal relationship between the beneficiary and the bank is formed when the bank confirms the letter of credit, and this relationship is not a third contract. The bank will act as accepting drafts, negotiating, or paying the beneficiary once the complying documents are presented to it (Busto, 1993, p. 24).

[9] See Chapter III.3.3.1 and Chapter IV.4.2.3 for further information about the payment and the banks' obligations.

This letter of credit is not a contract, but rather a separate and independent agreement between the buyer's bank (the issuing bank) and the seller. The letter of credit is a binding legal agreement that sets out the terms and conditions under which the seller will be paid by the issuing bank, provided that the seller meets the specified conditions in the letter of credit, such as presenting compliant documents.

While the buyer and seller are parties to the underlying commercial transaction, they do not typically have a direct contractual relationship with each other under the letter of credit. Instead, the letter of credit serves as a guarantee of payment by the issuing bank to the seller which is automatically triggered once the issuing bank announces to their beneficiary about the issuance of the letter of credit. Therefore, it would be more accurate to say that the letter of credit is a separate and independent agreement between the issuing bank and the seller. However, the letter of credit does play a critical role in facilitating the underlying commercial transaction between the buyer and seller and is a legally binding document that must be carefully drafted and reviewed by all parties involved.

4.2.4. The Relationship between the Issuing Bank and the Correspondent Bank

In the letter of credit, the issuer might invite other banks into the progress of the letter of credit to perform on its behalf. These banks are called correspondent banks. This contractual relationship shall be bound once the correspondent bank is comprised in the letter of credit. The agreement between banks will include rights and duties as well as the requirements of the reimbursement duties of the issuer. The reimbursement must be made to the correspondent bank by the issuing bank once the correspondent bank makes the payment to the beneficiary (Gutteridge & Megrah, 1955, p. 43).

4.3. The Rights and Obligations of Parties

4.3.1. The Buyer’s Rights and Obligations

Because the focal point of this thesis is fraud rules, the author shall briefly illustrate the rights and obligations of the buyers and the sellers in the progress of letters of credit rather than giving the details of their obligations in the underlying contracts.

<u>In the underlying contract</u>

The “letter of credit” term in the sales contract must contain “sufficient particularity what the credit should be” (Jack, 1991, p. 33). The terms in the underlying contract must conform with the requirements in the letter of credit. For example, in the case law *Ficom SA v. Sociedad Cadex Limitada*, the dispute happened because of the differences between the terms in the letter of credit and the terms in the underlying contract (Ficom SA v. Sociedad Cadex Limitada, 1980). In the terms of the credit, the payment would not be made if the quality of the products were considered not qualified enough while the terms in the underlying contract stated that the buyer is not allowed to cancel the contract for the same reason. Moreover, the buyer could

reduce the price in some specific situations while the terms in the credit do not allow that (Ficom SA v. Sociedad Cadex Limitada, 1980).

The Court held that the parties must follow the requirements of the letter of credit. Justice Robert Goff stated:

> "[…] it follows that the seller could only draw on the letter of credit if they tendered a quality certificate in accordance with the requirements of the letter of credit so established." (Ficom SA v. Sociedad Cadex Limitada, 1980)

This case illustrates the unfortunate scenario where parties agreed on a contract but concluded different terms in the credit, causing the dispute in payment. Once the buyer fails to object to the controversial terms in the letter of credit and lets the terms be carried out, he loses his right to object later, and parties are bound by the terms of the credit (Ficom SA v. Sociedad Cadex Limitada, 1980)[10].

<u>At the opening time of the letter of credit</u>

According to the underlying contract's requirements, the letter of credit must be launched at the right time to trigger the performance of the seller, such as preparing or shipping goods. It is usually understood that the seller's liability to send the goods is linked to the duty to open the buyer's letter of credit. The date to open the letter of credit might be stated clearly on the underlying contract, or it could be depended on the conduct of the seller.

In the case *Garcia v. Page & Co. Ltd*, there was a failure to open a letter of credit by the buyer in May even though the parties had agreed on the opening period in the sales contract (Garcia v. Page & Co. Ltd, 1936). It was not until the beginning of September that the buyer opened the credit, and the Court interpreted the aforesaid condition in the credit as "the buyer must have such time as is needed by a person of reasonable diligence to get that credit established" (Garcia v. Page & Co. Ltd, 1936). Hence, the Court held that the seller was allowed to terminate the sales contract because of the failure of the buyer to request the opening of the letter of credit on time (Garcia v. Page & Co. Ltd, 1936).

The Court in the case *Pavia & Co. SPA v. Thurmann-Nielsen* again impressed the importance of the time to open the credit:

> "The seller is not bound to tell the buyer the precise date when he is going to ship; and whenever he does ship the goods, he must be able to draw on the credit." (Pavia & Co. SPA v. Thurmann-Nielsen, 1951)

[10] See more cases Panoutsos v. Raymond Hadley Corporation of New York ([1917] 2 KB 473); Soproma SPA v. marine and Animal By-Products Corporation ([1966] 1 Lloyd's Rep 367).

In case the underlying contract states the specific date for shipping, the letter of credit must be launched a moderate time before the shipping date (Schmitthoff, 2000, p. 186). The case *Glencore Grain Rotterdam BV. v Lebanese Organization for International Commerce* emphasizes the importance of opening a letter of credit on time again (Glencore Grain Rotterdam BV. v Lebanese Organization, 1997). There was a FOB term in the sales contract, and the buyer stated the exact name of the vessel to ship the goods. After the letter of credit was opened, the bank informed the seller that the payment could only be made if the seller had presented the "freight prepaid bill of lading" (Glencore Grain Rotterdam BV. v Lebanese Organization, 1997). The seller rejected such a condition but did not have any further communication with other parties regarding this issue. Later, the seller refused to ship the products and the buyer took the case to court (Glencore Grain Rotterdam BV. v Lebanese Organization, 1997).

Justice Longmore stated that "The sellers thereafter did not act inconsistently with their previous refusal, and their silence on this matter cannot be regarded as an acceptance of the buyer's demand." (Glencore Grain Rotterdam BV. v Lebanese Organization, 1997). Justice Evans further held that "It follows that the buyer failed to open a letter of credit conforming with the sale contract and, subject to the question of waiver considered below, they were thereby in breach of contract." (Glencore Grain Rotterdam BV. v Lebanese Organization, 1997).

As stated in the aforementioned cases, the seller is allowed to claim damage if the buyer fails to open the credit because the failure in opening the credit constitutes a breach of contract.

4.3.2. The Seller's rights and obligations

As has been stated, the seller must carefully examine the terms of the letter of credit. Hence, the ICC Guide to Documentary Credit Operations has a checklist that is recommended for the examinator to follow (Busto, 1994, p. 32).

The shipping obligation of the seller is considered to be triggered by the opening of letters of credit by the buyer[11]. In practice, the buyer rarely fails to open the credit, however, the letter of credit may contain terms that are not similar as they should be in the underlying contract. There might be possibilities as follows:

- The terms in the letter of credit are rejected by the seller and an amendment is taken after the parties discussed.
- The objection of the seller might not provoke the buyer's awareness, and the credit may not be amended. The non-conforming terms shall not be considered being accepted by the seller if he remains silent and gives no objection to (Glencore Grain Rotterdam BV. v Lebanese Organization, 1997).
- The seller might treat the non-conforming terms as if they were conformed terms.

[11] See Chapter IV.4.2.1. for further details on the opening of letters of credit.

In the amendment of the Irrevocable Credit

The terms in the letter of credit must be similar to the terms in the underlying contract. However, the applicant's instructions to the bank do not always reflect the requirements from the underlying contract, which results in differences between the letter of credit and the underlying contract. As has been stated, the binding relationship between the bank and the seller is formed once the bank issues the letter of credit. Hence, the amendment must be discussed among all parties. Article 10 of UCP 600 states that:

> "a. Except as otherwise provided by Article 38, a credit can neither be amended nor cancelled without the agreement of the issuing bank, the confirming bank, if any and the beneficiary.
> b. An issuing bank is irrevocably bound by an amendment as of the time it issues the amendment. A confirming bank may extend its confirmation to an amendment and will be irrevocably bound as of the time it advises the amendment. A confirming bank may, however, choose to advise an amendment without extending its confirmation and, if so, it must inform the issuing bank without delay and inform the beneficiary of its advice.
> c. The terms and conditions of the original credit (or a credit incorporating previously accepted amendments) will remain in force for the beneficiary until the beneficiary communicates its acceptance of the amendment to the bank that advised such amendment. The beneficiary should give notification of acceptance or rejection of an amendment. If the beneficiary fails to give such notification, a presentation that complies with the credit and any not yet accepted amendment will be deemed to be notification of acceptance by the beneficiary of such amendment. As of that moment, the credit will be amended.
> d. A bank that advises an amendment should inform the bank from which it received the amendment of any notification of acceptance or rejection.
> e. Partial acceptance of an amendment is not allowed and will be deemed to be notification of rejection of the amendment.
> f. A provision in an amendment to the effect that the amendment shall enter into force unless rejected by the beneficiary within a certain time shall be disregarded." (International Chamber of Commerce, 2007)

The applicant needs to require his bank to adjust the credit to avoid conflicts between the terms of the letter of credit and the terms in the underlying contract. Once the issuer considers the adjustments possible, they will notify the beneficiary about the proposed amendment. If there is an advising bank in the credit, the issuer shall notify the adviser and the adviser shall give instructions to the beneficiary. The confirming bank may also communicate with the beneficiary about the amendments in the confirmed credit. The confirmation before shall not extend to the amendment.

The amendment needs the approval of the beneficiary to be effective. The beneficiary might express their acceptance by submitting the documents conforming to the adjusted term of the

credit or giving the acceptance of the amendment explicitly. The silence of the beneficiary toward the amendment will not be understood as acceptance. In case the beneficiary does not agree with the amendment, he might inform the banks about his rejection.

In the amendment of the Revocable Credit

As has been stated, the issuing bank could amend or cancel the revocable letter of credit on any occasion without the beneficiary's consent.

In case the terms in the Letter of Credit conflict with the terms in the Underlying Contract

Sometimes the terms in the letter of credit opened by the bank might be different from the terms as parties agree in the sales contract in practice. Rather than claiming the damages and cancelling the contract, the seller keeps conducting the letter of credit and hoping that the buyer will perform his duties.

This conduct might have different consequences. The buyer either totally performs his duties in the sales contract and the parties will have a "happy ending ever after" or the buyer might be unsuccessful in performing the duties described in the underlying contract or find out that the obligations of the seller in the underlying contract are not fully performed and bring the case to the courts claiming for breaching of contract. To respond, the seller might claim that the terms in the credit do not follow the requirements in the underlying contract, hence, he is not obligated to follow the requirements. This response will probably raise scenarios where the court either holds opinions that the seller has waived the discrepancies or tells the seller that he is no longer available to complain about it.

In the leading case *Panoutsos v. Raymond Hadley Corporation of New York*, an unconfirmed credit was opened by the bank meanwhile according to the requirement, it should open a confirmed letter of credit (Panoutsos v. Raymond Hadley Corporation of New York, 1917). The seller did not reject the unconfirmed credit when they got a notification. Furthermore, they asked for a delay for the credit and got accepted. The seller later claimed to cancel the underlying contract because there were differences between the terms in the contract and the letter of credit. The holding of the Court of Appeal stated that: "[t]he seller, by waiving for a time the condition as to a confirmed credit, was not thereby bound to act upon that credit up to the end of the contract, but that he was not entitled to cancel the contract without giving the buyer reasonable notice of his intention to cancel to give the buyer the opportunity of complying with the conditions." (Panoutsos v. Raymond Hadley Corporation of New York, 1917).

This point of view is once again confirmed in the case *Plasticmoda Societa per Azioni v. Davidsons (Manchester) Ltd.* when Lord Denning stated that "[i]f one party, by his conduct, leads another to believe that the strict rights arising under the contract will not be insisted upon, intending that the other should act on that belief, and he does act on it, then the first party will

not afterwards be allowed to insist on the strict rights when it would be inequitable for him so to do." (Plasticmoda Societa per Azioni v. Davidsons (Manchester) Ltd., 1952).

The other response of the courts is explained in the case *WJ Alan & Co Ltd. v. El Nasr Export*. Parties agreed to use a confirmed irrevocable letter of credit as payment method (WJ Alan & Co Ltd. v. El Nasr Export, 1972). Unfortunately, the letter of credit had several terms that did not conform with the sales contract's terms. The seller did not object to the credit and carried on their obligations under the credit and received the sterling (not the Kenya Shillings as agreed in the underlying contract). Unfortunately, the sterling lost its value and the seller asked for additional 165,530.45 Kenya Shillings from the buyer to cover the devaluation of the sterling currency (WJ Alan & Co Ltd. v. El Nasr Export, 1972). Lord Megaw made clear that "The sellers accepted that offer by making use of the credit to receive payment for a part of the contractual goods. By that acceptance, as the sellers must be deemed to have known, not only did the confirming bank become irrevocably bound by the terms of the offer (and by no other terms), but so also did the buyers become bound." (WJ Alan & Co Ltd. v. El Nasr Export, 1972)

In the presentation of Documents

It is the responsibility of the seller to submit the documents complying with the requirements of the letter of credit to receive payment. Under Article 33 of UCP 600, the presentation should be made while the credit is valid and during banking hours (International Chamber of Commerce, 2007), and the documents presented are "in accordance with the terms and conditions of the credit, and not, on their face, inconsistent with one another." (Busto, 1994, p. 33). Furthermore, the presentation time of the documents must be "on or before the expiry day" as stated in Article 6(e) of UCP 600 (International Chamber of Commerce, 2007). Once the credit requires for the transportation documents, the letter of credit must clearly state the certain period for presenting the transportation documents considering Article 31 of UCP 600 (International Chamber of Commerce, 2007).

4.3.3. The Bank's rights and obligations

A. The Issuing Bank

In Accepting the Instructions of the Applicant

As agreed in the underlying contract, the buyer will apply to his bank to open a letter of credit in favour of the seller. Once the bank accepts the application, a contractual agreement shall be formed between the bank and its customer. The importance of the specific instructions in the application is described above[12]. However, there are risks that such instructions sometimes might be not well-constructed or not conform with the bank's policies, etc. Hence, according

[12] See Chapter IV.4.2.1 and IV.4.2.2. for further information about the relationships between parties.

to Article 7 of UCP 600[13], the bank is trusted to reduce these risks by including more specific details in letters of credit as well as giving instructions to issuing, advising, or confirming to other banks in letters of credit in case there are other banks invoked in the letter-of-credit transaction (International Chamber of Commerce, 2007). Since the bank is bound when the credit is issued, the content of the credit must be well-drafted (International Chamber of Commerce, 2007), and any unclear or contradicted terms should not remain in the credit. As stated in Article 9 of UCP 600, once there are any amendments in the credit, it is only valid with the consent of the beneficiary (International Chamber of Commerce, 2007).

In case there are ambiguous terms, the view of the English Courts is to take the side which allows the banks to interpret the terms at a moderate level and considers the documents "accord with the true construction of the credit" (Jack, 1991, p. 62). This orientation is clearly expressed in the case *Midland Bank v. Seymour*. The plaintiff claimed the accepted bill of lading did not comply with the terms and conditions in the letter of credit since there were no full descriptions of the goods, quality as well as price, and weight while parties agreed that such descriptions must be added (Midland Bank v. Seymour, 1955). The Court considered that the bank should act reasonably because the letter of credit should state clearly what kind of documents are needed with exact information in every document. The Court stated that "no principle is better established than that when a banker … is given instructions …, they must be given to him with reasonable clearness. The banker is obliged to act upon them precisely." (Midland Bank v. Seymour, 1955)

The picture is further explained in the case Commercial Banking Co. of Sydney Ltd. v. Jalsard Pty. Ltd. The Court held that:

> "Both the issuing banker and his correspondent bank have to make quick decisions as to whether a document which has been tendered by the seller complies with the requirements of the credit at the risk of incurring liability to one or other of the parties to the transaction if the decision is wrong. Delay in deciding may in itself result in a breach of his contractual obligations to the buyer or the seller. This is the reason for the

[13] Article 7 of UCP 600 provides:
"Issuing Bank Undertaking
a. Provided that the stipulated documents are presented to the nominated bank or to the issuing bank and that they constitute a complying presentation, the issuing bank must honour if the credit is available by:
i. sight payment, deferred payment, or acceptance with the issuing bank;
ii. sight payment with a nominated bank and that nominated bank does not pay;
iii. deferred payment with a nominated bank and that nominated bank does not incur its deferred payment undertaking or, having incurred its deferred payment undertaking, does not pay at maturity;
iv. acceptance with a nominated bank and that nominated bank does not accept a draft drawn on it or, having accepted a draft drawn on it, does not pay at maturity;
v. negotiation with a nominated bank and that nominated bank does not negotiate. b. An issuing bank is irrevocably bound to honour as of the time it issues the credit.
c. An issuing bank undertakes to reimburse a nominated bank that has honoured or negotiated a complying presentation and forwarded the documents to the issuing bank. Reimbursement for the amount of a complying presentation under a credit available by acceptance or deferred payment is due at maturity, whether or not the nominated bank prepaid or purchased before maturity. An issuing bank's undertaking to reimburse a nominated bank is independent of the issuing bank's undertaking to the beneficiary."

rule that where the banker's instructions from his customer are ambiguous or unclear he commits no breach of his contract with the buyer if he has construed them in a reasonable sense, even though upon closer consideration which can be given to questions of construction in an action in a court of law, it is possible to say that some other meaning is to be preferred." (Commercial Banking Co. of Sydney Ltd. v. Jalsard Pty. Ltd., 1972)

In The Issuance of Letters of Credit

The bank shall open the letter of credit once it receives and accepts the instructions from the applicant. The duties of the bank shall be bound at the time it opens the letter of credit as well. The term "open" is understood as the stage when the bank communicates with the beneficiary about the documentary credit.

There shall be two ways out for the bank if they fail to follow the commands of the applicant:

- The Bank might be responsible for the breach of contract; or
- The Bank might lose its right to reimbursement if it receives the documents complying with the non-conforming letter of credit.

The opinion of the courts regarding such circumstances is that the bank might lose its right to reimbursement if there are any failures in complying with the applicant's instructions.

In Letters of Credit Forms

In UCP 600, letters of credit do not need to be in any specific forms, however, the term "text" in Article 1 of UCP 600[14] is mainly relevant to the writing form. Furthermore, the ICC has taken care of the form of documentary credit by issuing a standard form. Such form is generally applied in most international transactions without modification (Busto, 1993).

In the Examination of Documents

Under Article 14(a) of UCP 600, the documents are necessitated to be examined by the bank "to determine, based on the documents alone, whether or not the documents appear on their face to constitute a complying presentation." (International Chamber of Commerce, 2007).

According to Article 15(a) of UCP 600[15], the bank shall examine the confirmed credit and when they find the documents meet the requirements, "it must honour" (International Chamber

[14] Article 1 of UCP 600 provides:
"Application of UCP
The Uniform Customs and Practice for Documentary Credits, 2007 Revision, ICC Publication no. 600 ("UCP") are rules that apply to any documentary credit ("credit") (including, to the extent to which they may be applicable, any standby letter of credit) when the text of the credit expressly indicates that it is subject to these rules. They are binding on all parties thereto unless expressly modified or excluded by the credit."
[15] Article 15(a) of UCP 600 provides:

of Commerce, 2007). Otherwise, the bank may "refuse to honour or negotiate" in light of Article 16(a)[16] (International Chamber of Commerce, 2007). In this circumstance, the documents shall be sent back to the presenter and the bank will "give a single notice to that effect to the presenter" (International Chamber of Commerce, 2007). However, according to Article 16(b) of UCP 600, the issuing bank might "in its sole judgment approach the applicant for a waiver of the discrepancies" (International Chamber of Commerce, 2007).

When the documents are decided to conform to the requirements, the bank either pays or negotiates and sends the documents to the applicant as stated in Article 15(b) of UCP 600 (International Chamber of Commerce, 2007). Otherwise, considering Article 16(c) of UCP 600, once the issuer found any discrepancies, they shall immediately notify the presenter ((International Chamber of Commerce, 2007).

Under Article 16(c) of UCP 600, the single notice of rejection must state every discrepancy and be sent just once. In case there are several notices regarding the discrepancies, only the first notice is valid (International Chamber of Commerce, 2007). Moreover, the notice must be given by any kind of communication method "no later than the close of the fifth banking day following the day of presentation" according to Article 16(d)[17] (International Chamber of Commerce, 2007) and by any chances, the banks fail to inform any discrepancies on time, complete and properly as a "single notice", they shall lose their right to claim the documents are non-conforming (International Chamber of Commerce, 2007).

In Waiver of Discrepancies

The issuing bank shall have two obligations arising from the submission of documents. First, the banks must check the submitted documents whether on their face conform to the requirements of the credit. Second, they should decide what to do if the stipulated documents have discrepancies (Buckley, 1995, p. 269). There are always chances that the documents probably have discrepancies (International Chamber of Commerce, 2007)[18] (Mann, 2000, p. 2495)[19]. As mentioned, due to the principles of letters of credit, the banks could refuse

"a. When an issuing bank determines that a presentation is complying, it must honour."

[16] Article 16 of UCP 600 provides:
"Discrepant Documents, Waiver and Notice
a. When a nominated bank acting on its nomination, a confirming bank, if any, or the issuing bank determines that a presentation does not comply, it may refuse to honour or negotiate.
b. When an issuing bank determines that a presentation does not comply, it may in its sole judgement approach the applicant for a waiver of the discrepancies. This does not, however, extend the period mentioned in sub-article 14 (b).
c. When a nominated bank acting on its nomination, a confirming bank, if any, or the issuing bank decides to refuse to honour or negotiate, it must give a single notice to that effect to the presenter."

[17] Article 16(d) of UCP 600 provides:
"d. The notice required in sub-article 16 (c) must be given by telecommunication or, if that is not possible, by other expeditious means no later than the close of the fifth banking day following the day of presentation. "

[18] The Introduction of the UCP 600 states that "When work on the revision started, a number of global surveys indicated that, because of discrepancies, approximately 70% of documents presented under letters of credit were being rejected on the first presentation."

[19] In the interview with the bankers in the survey of Professor Mann, there are claims that the presenters "do not present documents that conform to the requirements of the letter of credit".

presented documents if they know the discrepancies in such a set of documents. Consequently, the beneficiary will not receive their payment. However, the beneficiary can still be paid by the applicant's waiver for the discrepant documents. Such waiver of documentary imperfections will be given by the issuing bank's enquiry to the applicant (Mann, 2000, pp. 2513-2514)[20] (Moses, 2003, pp. 484-489).

The applicant waiver for documentary defects normally happens with commercial letters of credit. Due to its special conditions, the commercial credits usually ask for a set of different documents and such documents are more complicated than the standbys, which increases a higher chance of discrepancies (Dolan, 1996, pp. 1-3). Compared to the standby credit, the applicant in the commercial one wants the goods in the contract for sale and has economic motivations to waive the discrepancies in such documents. On the contrary, the applicant in the standby obtains nearly nothing from his waiver, his only obligation is to reimburse the issuer (Byrne, 1998).

Under Article 14 (d) and Article 16 (a) of UCP 600, the banks must detect and notice the discrepancies in the stipulated documents under a prompt notice to the presenter (International Chamber of Commerce, 2007). As has been stated, such rules are backed up by the main principles of the letter of credit law, the financial practice (International Chamber of Commerce, 2007), and the judgments (Fidelity Nat'l Bank v. Dade County, 1979) (AMF Head Sports Wear, Inc. v. Ray Scott's All-Am. Sports Club, 1978) (Courtaulds No. Am., Inc. v. North Carolina Nat. Bank, 1975) (Equitable Trust Co. of New York v. Dawson Partners, Ltd., 1927). Such cases provide that the banks must follow the guidance of the applicant and honour the credit in only cases that the presented documents on their face rigidly conform to the requests in the credit issued by the banks.

In examining the genuine of the documents

Article 14(a) of UCP 600 expects the bank to honour the tendered documents if they "on their face" meet the requirements under the letter of credit. As a result, the bank is not bound to invest in the facts that happened beyond the documents to clarify whether the documents are legitimate or fraudulent. In case the applicant accuses a certain document is forged, he will bear the burden to prove his allegation to the courts.

Article 34 of UCP 600 states that:

> "A bank assumes no liability or responsibility for the form, sufficiency, accuracy, genuineness, falsification or legal effect of any document, or for the general or particular conditions stipulated in a document or superimposed thereon; nor does it assume any liability or responsibility for the description, quantity, weight, quality, condition, packing, delivery, value or existence of the goods, services or other

[20] According to the survey of Professor Mann, applicants normally waive discrepancies even though there are defaults in the underlying contract.

> performance represented by any document, or for the good faith or acts or omissions, solvency, performance or standing of the consignor, the carrier, the forwarder, the consignee or the insurer of the goods or any other person." (International Chamber of Commerce, 2007)

The ICC also expressed that the authenticity of the documents is beyond the scope of UCP:

> "If a document appears of original or to have been marked as original but is in fact not original, then its presentation may give rise to exceptional defences, rights, or obligations under the law applicable to forged or fraudulent presentation […]" (Commission on Banking Technique and Practice, 1999).

Force majeure

Article 36 of UCP 600 signifies the risks of force majeure as:

> "A bank assumes no liability or responsibility for the consequences arising out of the interruption of its business by Acts of God, riots, civil commotions, insurrections, wars, acts of terrorism, or by any strikes or lockouts or any other causes beyond its control. A bank will not, upon resumption of its business, honour or negotiate under a credit that expired during such interruption of its business." (International Chamber of Commerce, 2007)

As we can understand in the light of Article 36, the bank is released from its obligation in case the presented documents are not available due to the aforementioned circumstances. The bank is also discharged from its undertaking once the credit is expired during "such interruption" (International Chamber of Commerce, 2007).

In the duty to pay

The payment duty of the issuing bank is triggered once the tendered documents are decided to conform to the requirements. The bank must prepare the payment on the scheduled date as agreed under the credit. If the payment date falls on the non-banking day, then according to Article 29(a)[21], "the expiry date or the last day for presentation, as the case may be, will be extended to the first following banking day" (International Chamber of Commerce, 2007).

B. The Correspondent Bank

In basic typical letters of credit, there is only one bank included in the transaction called the issuing bank which is the bank of the buyer. However, the issuing bank normally wants to

[21] Article 29(a) of UCP 600 provides:
"a. If the expiry date of a credit or the last day for presentation falls on a day when the bank to which presentation is to be made is closed for reasons other than those referred to in article 36, the expiry date or the last day for presentation, as the case may be, will be extended to the first following banking day."

invite other banks into the transaction to communicate with the beneficiary, especially when the beneficiary locates in a different country from the issuing bank. These banks are referred to as the "correspondent banks" and may perform under the following names:

- Advising bank: the bank advises letters of credit.
- Confirming bank: the bank confirms letters of credit.
- Nominated bank: the bank pays, accepts drafts, or negotiates the documents of letters of credit.

The Advising Bank

In the credit transaction including other banks, these banks shall be assigned by the issuing bank. The added second bank shall be called an advising bank (or the "adviser") if it is not required to authorize or confirmed the credit or refuses to do so.

The advising bank's main function is to validate letters of credit and send the documents to the issuing bank. Such a bank bears no burden to affect the settlement for the beneficiary since this responsibility still belongs to the issuing bank. According to Article 9 of UCP 600, the accountabilities of the advising bank are clearly described as follows:

> "a. A credit and any amendment may be advised to a beneficiary through an advising bank. An advising bank that is not a confirming bank advises the credit and any amendment without any undertaking to honour or negotiate.
> b. By advising the credit or amendment, the advising bank signifies that it has satisfied itself as to the apparent authenticity of the credit or amendment and that the advice accurately reflects the terms and conditions of the credit or amendment received.
> c. An advising bank may utilize the services of another bank ("second advising bank") to advise the credit and any amendment to the beneficiary. By advising the credit or amendment, the second advising bank signifies that it has satisfied itself as to the apparent authenticity of the advice it has received and that the advice accurately reflects the terms and conditions of the credit or amendment received.
> d. A bank utilizing the services of an advising bank or second advising bank to advise a credit must use the same bank to advise any amendment thereto." (International Chamber of Commerce, 2007)

In case the documentary credit expresses that the documents must be handed over to the advising bank, the bank shall perform as a forwarder to give the documents to the issuer. In such circumstances, the adviser has no liability to pay. Otherwise, the advising bank might be expressed as a selected bank in the documentary credit. In such a case, the advising bank shall receive and examines the documents, and then pay for the beneficiary.

The duties of the advising bank are depended on the types of credit as such:

- Sight credit: the bank shall pay upon the documents' examination.

- Deferred payment credit: the settlement shall be affected after the documentary examination when the draft is drawn on the bank. Otherwise, the documents will be sent to the issuer.
- Negotiable credit: the bank shall pay immediately with a discount price.

In some circumstance, the adviser shall collect the documents and sends them to the issuer. In such a situation, the adviser is the collecting bank. The collecting bank will inspect the conformity of the documents before sending them to the issuer (Jack, 1991, p. 128).

The Confirming Bank

Under Article 8 of UCP 600, the confirming bank is expressed as:

> "a. Provided that the stipulated documents are presented to the confirming bank or to any other nominated bank and that they constitute a complying presentation, the confirming bank must:
> i. honour, if the credit is available by
> a. sight payment, deferred payment, or acceptance with the confirming bank.
> b. sight payment with another nominated bank and that nominated bank does not pay;
> c. deferred payment with another nominated bank and that nominated bank does not incur its deferred payment undertaking or having incurred its deferred payment undertaking does not pay at maturity.
> d. acceptance with another nominated bank and that nominated bank does not accept a draft drawn on it or, having accepted a draft drawn on it, does not pay at maturity.
> e. negotiation with another nominated bank and that nominated bank does not negotiate.
> ii. negotiate, without recourse, if the credit is available by negotiation with the confirming bank.
> b. A confirming bank is irrevocably bound to honour or negotiate as of the time it adds its confirmation to the credit.
> c. A confirming bank undertakes to reimburse another nominated bank that has honoured or negotiated a complying presentation and forwarded the documents to the confirming bank. Reimbursement for the amount of a complying presentation under a credit available by acceptance or deferred payment is due at maturity, whether or not another nominated bank prepaid or purchased before maturity. A confirming bank's undertaking to reimburse another nominated bank is independent of the confirming bank's undertaking to the beneficiary.
> d. If a bank is authorized or requested by the issuing bank to confirm a credit but is not prepared to do so, it must inform the issuing bank without delay and may advise the credit without confirmation." (International Chamber of Commerce, 2007)

According to Article 8(b) of UCP 600, it can be interpreted that the confirming banks are bound by their promises to pay or to negotiate by the time they agree to confirm the credit (International Chamber of Commerce, 2007). Hence, the confirming banks' duties are separate from the issuer and are dependent as well (Busto, 1993, p. 24). The confirming bank must

examine the credit and they will honour the documents if such documents facially conform to the requirements in the credit. In case the documents are found with discrepancies, the confirming bank shall refuse and inform the presenter according to Article 8(d) of UCP 600 (International Chamber of Commerce, 2007). In some circumstances, the confirming bank might reach the issuing bank for further instructions, and the issuing bank shall have further act as stated in Article 16 of UCP 600 (International Chamber of Commerce, 2007).

The Nominated Bank

Under Article 1 of UCP 600, the nominated bank is "the bank with which the credit is available or any bank in the case of a credit available with any bank." (International Chamber of Commerce, 2007). The nominated bank could be the issuer or any other bank due to the requirements of the parties. According to Article 12 of UCP 600[22], once the nominated bank agrees with the authorization to honour or to negotiate with the beneficiary, the nominated bank could pay, accept, or negotiate against conformed documents (International Chamber of Commerce, 2007).

Reimbursement of the Correspondent Bank

One of the main obligations of the issuer is to reimburse the correspondent bank when such a bank accepts, pays, or negotiates the documents considering Article 13 of UCP 600 (International Chamber of Commerce, 2007). Under Article 13 of UCP 600[23], the correspondent bank shall get their reimbursement from the issuer in case the correspondent bank takes the documents, considers the documents as complying, and effects settlement.

[22] Article 12(b) of UCP 600 provides:
"b. By nominating a bank to accept a draft or incur a deferred payment undertaking, an issuing bank authorizes that nominated bank to prepay or purchase a draft accepted or a deferred payment undertaking incurred by that nominated bank."

[23] Article 13(b) of UCP 600 provides:
"b. If a credit does not state that reimbursement is subject to the ICC rules for bank-to-bank reimbursements, the following apply:
i.An issuing bank must provide a reimbursing bank with a reimbursement authorization that conforms with the availability stated in the credit. The reimbursement authorization should not be subject to an expiry date.
ii.A claiming bank shall not be required to supply a reimbursing bank with a certificate of compliance with the terms and conditions of the credit.
iii.An issuing bank will be responsible for any loss of interest, together with any expenses incurred, if reimbursement is not provided on first demand by a reimbursing bank in accordance with the terms and conditions of the credit.
iv.A reimbursing bank's charges are for the account of the issuing bank. However, if the charges are for the account of the beneficiary, it is the responsibility of an issuing bank to so indicate in the credit and in the reimbursement authorization. If a reimbursing bank's charges are for the account of the beneficiary, they shall be deducted from the amount due to a claiming bank when reimbursement is made. If no reimbursement is made, the reimbursing bank's charges remain the obligation of the issuing bank."

CHAPTER V

ACCOMPANYING DOCUMENTS

As has been stated, there are plenty of risks in international trade, especially when the merchants need to transfer the goods through borders or even through the sea. The risks might be geography, different cultures, or differences in legal legislation. The seller is afraid of not receiving payment once he sends the goods away. The buyer, in another hand, wants to pay for the goods and wants to assure that he gets the goods as described in the sales contract. Hence, a letter of credit is added to the transactions to minimize such risks among parties. Letters of credit solve these risks by including an adequate list of documents that the buyer needs to receive the goods and guarantee that the seller shall get his payment by submitting the complying documents.

The applicant shall provide a list of documents he needs to possess the goods and these documents also present the guarantee of the quality and quantity of the goods before shipping. This list provides security for the buyer to ensure the seller will fulfil his obligations under the contract. On the other side, the seller is also protected by the letter of credit since he is assured that he will receive payment once he presents the exact documents listed in the letter of credit complying with the requirements in the letter of credit.

5.1. General requirements

Strict compliance[24]

The documents are required to be presented as strictly conform to the requests in the letter of credit. Such compliance is one of the cornerstone rules of letters of credit. As Lord Sumner in the *Equitable Trust Co. of New York v. Dawson Partners*:

> "There is no room for documents which are almost the same, or which will do just as well. The business could not proceed securely on any other lines." (Equitable Trust Co. of New York v. Dawson Partners, Ltd., 1927)

The discrepancies might happen in the content of the documents, but such discrepancies must not represent the existing good value or could be typography. According to Article 16 of UCp 600, the banks nonetheless must adopt the guidance from their applicants and reject the discrepant documents unless the applicant gives another instruction (International Chamber of Commerce, 2007).

Consistency

[24] See Chapter VI.6.2 for further information about the Strict Compliance Principle.

The requirement of consistency is illustrated in the case of *Soproma S.p.A v. Marine & Animal BY- Products Corporation*. In this case, the sales contract required the documents of the goods must describe the goods as "…full meal, steam dried, minimum 70% protein…" (Soproma S.p.A v. Marine & Animal BY- Products Corporation, 1966). However, some of the presented documents (which were the commercial invoice, analysis certificate, and bill of lading) showed differences in describing the products. Hence, the Court ruled that the presented documents had not been "a good tender" since the documents were not consistence with each other (Soproma S.p.A v. Marine & Animal BY- Products Corporation, 1966).

The Banking Commission of ICC expressed their opinion about the consistency of the documents as follows:

> "The notion of 'consistency'… should be understood as meaning that the whole of the documents must obviously relate to the same transaction, that is to say, that each should bear a relation with the others on the face, and the documents should not be inconsistent with one another". (ICC Banking Commission, 1980).

The Origin of Documents

Presenting original documents is a basic requirement under letters of credit unless they state differently. However, modern technology might confuse bank examiners in finding authentic documents. It could be a challenge for bank examiners to decide whether the presented documents are copy versions or printed ones. Such issues shall create uncertainty for letters of credit and might create disputes about the authentication of the documents. The efficiency of this instrument will be reduced as a result. Hence, Article 17(c) of UCP 600[25] decides to establish a clear mechanism to treat the documents in a certain way which they should be treated.

As has been stated in Article 17(c), the documents listed in this article are considered original unless there are different instructions. The confusion between the original and the copies might be illustrated in the following cases[26].

The case *Glencore International A.G. and Bayerische Vereinsbank A.G. v. Bank of China* raised a question regarding the origin of the documents. In this case, there were two letters of credit issued by the Bank of China, requiring several documents including a certificate of origin. The certificates of the beneficiary were rejected by the Bank of China and the Bank stated that under the light of Article 20(b) of UCP 500[27], the presented documents "were neither

[25] Article 17(c) of UCP 600 provides:
"Unless a document indicates otherwise, a bank will also accept a document as original if it:
i. appears to be written, typed, perforated, or stamped by the document issuer's hand; or
ii. appears to be on the document issuer's original stationery; or
iii. states that it is original, unless the statement appears not to apply to the document presented."
[26] These cases are applied with the UCP 500; however, the author thinks it is worth to mention.
[27] Article 20(b) of UCP 500 provides:

original documents nor… marked original". (Glencore International A.G. and Bayerische Vereinsbank A.G. v. Bank of China, 1995). The documents were then proven by Glencore that they were photocopied in the required number, and both the photocopy machine and the printer used the same plain white paper, "it is impossible by the ordinary eye to distinguish the printed and the photocopied versions one document." (Glencore International A.G. and Bayerische Vereinsbank A.G. v. Bank of China, 1995). One of the documents was then signed by "ball-point pen… for the purpose of submission under the relevant letter of credit". It was further stated that "although the document tendered is in one sense a copy, for it was produced by reprographic means, in another sense it is an original, for it is the only version of the document to bear an original handwritten signature" (Glencore International A.G. and Bayerische Vereinsbank A.G. v. Bank of China, 1995).

Under the holding of the Trial Court, the allegation of the plaintiff was rejected. The Trial Court considered that "the production of the document is one thing, and its subsequent marking is another" (Glencore International A.G. and Bayerische Vereinsbank A.G. v. Bank of China, 1995). The Appeal Court then supported the previous decision and expressed that "a signature on a copy does not make an original, it makes an authenticated copy; and Art 20(b) does not treat a signature as a substitute for a marking as "original", merely as an additional requirement in some cases." (Glencore International A.G. and Bayerische Vereinsbank A.G. v. Bank of China, 1995).

The case *Kredietbank Antwerp v. Midland Bank PLC* also raises the question regarding the "original documents" (Kredietbank Antwerp v. Midland Bank PLC, 1999). In this case, the insurance documents were not marked as the original. In the trial, it was said that the insurance document was drafted on a computer and then printed on a sheet of paper that already had a blue ink headline by a laser printer. Then they photocopied the printed one. Hence, there was a clear difference between the printed and the copied one.

The Court held that the document prepared by the computerized system falls under Art 20(b) of UCP 500. Following the reason given in the Glencore case, such documents should be stamped "original" (Glencore International A.G. and Bayerische Vereinsbank A.G. v. Bank of China, 1995). In certain circumstances where the documents proved that they were original (such as the paper had original blue coloured logo of the company), then the documents did not have to be stamped original. By all statements, the court then ruled that the original documents do not fall under Article 20(b) of UCP 500 (Kredietbank Antwerp v. Midland Bank PLC, 1999).

"Unless otherwise stipulated in the Credit, banks will also accept as an original document(s), a document(s) produced or appearing to have been produced:
(i) by reprographic, automated or computerized systems.
(ii) as carbon copies; provided that it is marked as original and, where necessary, appears to be signed. A document may be signed by handwriting, by facsimile signature, by perforated signature, by stamp, by symbol, or by any other mechanical or electronic method of authentication."

However, this judgment was criticized by commentators since to examine the "obviously original", the test required the investigation of the bank in how the documents were produced (Johnson, 1999, p. 287) (Archer & Swallow, 1999) (Kredietbank Antwerp v. Midland Bank PLC, 1999). After receiving several questions relating to the original documents, a policy statement had been issued by the ICC Banking Commission which determined the precise interpretation as follows:

> "Banks treat as original any document bearing an apparently original signature, mark, stamp, or label of the issuer of the document unless the document itself indicates that it is not original. Accordingly, unless a document indicates otherwise, it is treated as original if it:
> (a) appears to be written, typed, perforated, or stamped by the document issuer's hand; or
> (b) appears to be on the document issuer's original stationery; or
> (c) states that it is original unless the statement appears not to apply to the document presented (e.g. because it appears to be a photocopy of another document and the statement of originality appears to apply to that other document)." (Commission on Banking Technique and Practice, 1999, p. 3)

The Issuer of the Documents

Those who can issue the transport document, insurance document, and commercial invoice are expressed clearly in Articles 18, 19, 20 21 and 22 of UCP 600 (International Chamber of Commerce, 2007). The required parties must be stated explicitly in the documents, otherwise, the banks shall take the documents in their current form and note that the submitted documents' information is not consistent with other presented documents (International Chamber of Commerce, 2007).

Issuance date

According to Article 14(i) of UCP 600:

> "A document may be dated prior to the issuance date of the credit but must not be dated later than its date of presentation." (International Chamber of Commerce, 2007)

This rule was first drafted in the UCP 1983 Revision (UCP 400) claiming that "shipping documents bearing a date of issuance prior to that of the documentary credit should be accepted" (ICC Banking Commission, 1980). In case the prior date of the documents is not accepted by the applicant, he must give the bank explicit guidance in this regard.

Article 3 of UCP 600 states further about the dating terminology:

> “The expression "on or about" or similar will be interpreted as a stipulation that an event is to occur during a period of five calendar days before until five calendar days after the specified date, both start and end dates included.
> The words "to", "until", "till", "from" and "between" when used to determine a period of shipment include the date or dates mentioned, and the words "before" and "after" excluding the date mentioned.
> The words "from" and "after" when used to determine a maturity date exclude the date mentioned.
> The terms "first half" and "second half" of a month shall be construed respectively as the 1st to the 15th and the 16th to the last day of the month, all dates inclusive.
> The terms "beginning", "middle" and "end" of a month shall be construed respectively as the 1st to the 10th, the 11th to the 20th, and the 21st to the last day of the month, all dates inclusive.” (International Chamber of Commerce, 2007)

5.2. Transportation documents

Geography distancing is one of the common problems along with the language and local commercial usage in international trade. Hence, transportation is considered the element to connect the countries and as time goes by, it requires development (Wheble, 1995).

The transportation documents have two different kinds of forms:

- The contract of the carrier and the shipper; or
- The receipt of the goods by the carrier.

The UCP 600 recognizes several different types of transport documents that banks may accept:

- Bill of lading[28]
- Non-negotiable seaway bill[29]
- Charter Party Bill of Lading[30]
- Air Transport Document[31]
- Road, rail, or inland waterway transport documents[32]
- Courier receipt, Post receipt, or Certificate of Posting[33]
- On Deck", "Shipper's Load and Count", "Said by Shipper to Contain" and Charges Additional to Freight[34]
- Clean Transport Document[35].

5.2.1. Bill of Lading

[28] Article 20 of UCP 600
[29] Article 21 of UCP 600
[30] Article 22 of UCP 600
[31] Article 23 of UCP 600
[32] Article 24 of UCP 600
[33] Article 25 of UCP 600
[34] Article 26 of UCP 600
[35] Article 27 of UCP 600.

The bill of lading is an essential document in international commerce because it is not only a receipt stating the quantity of the goods and the nature of the cargo, but it is also a document of title. The history of the bill of lading is traced back to the 14th century with the bill of lading's original form (Bennet, 2018) (McLaughlin, 1926). The case *Lickbarrow v. Mason* is quoted several times to express the mercantile usage of the bill of lading. The Court in this case had recognized the bill of lading as a document of the title since the property of the goods was transferred at the time the bill of lading was delivered to (Lickbarrow v. Mason, 1790).

The most important document regarding the harmonization of the bills of lading is the International Convention for the Unification of Certain Rules of Law Relating to Bills of Lading, known as "Hague Rules", in 1924[36] and later was revised in 1968 and now is known as the Hague-Visby Rules.

Later, the developing countries needed a new convention, hence, the UNCITRAL drafted the United Nations Convention on the Carriage of Goods by Sea, which is now known as the "Hamburg Rules", and it came into force in 1992. The Convention is still applied today in over 30 countries[37].

On the 34th session of the UNCITRAL in 2001, they decided to form a Working group to draft an instrument for the carriage of goods by sea. This Working group was formed with the CMI[38], FIATA[39], BIMCO[40], ICC, and ICS[41] (UN Secretary General, 2001)[42].

Later, due to the transportation improvement, the intention to provide a modern solution for international carriage and "including the growth of containerization, the desire for door-to-door carriage under a single contract, and the development of electronic transport documents", a new convention was accepted by the General Assembly on 11 December 2008. This convention is called the United Nations Convention on Contracts for the International Carriage of Goods Wholly or Partly by Sea or known as the "Rotterdam Rules" (UNCITRAL Working Group III (Transport Law), 2008) [43].

There are three main functions of the bill of lading which are:

- A receipt proving that the ship owner has received the goods.
- Proof of contract between the shipper and the carrier.
- A document of title allows the entitled person to handle the goods while transferring.

[36] It entered into force on 2 June 1931.
[37] See more at http://www.uncitral.org.
[38] CMI stands for Committee Maritime International.
[39] FIATA stands for International Federation of Freight Forwarders.
[40] BIMCO stands for Baltic and International Maritime Council.
[41] ICS stands for International Chamber of Shipping.
[42] See more at https://digitallibrary.un.org/record/446493?ln=en.
[43] See more at https://uncitral.un.org/en/texts/transportgoods/conventions/rotterdam_rules.

The bill of lading can be either non-negotiable (or straight, which does not allow the entitled person to transfer the goods to the other party by endorsement) or negotiable (means the products could be transferred by endorsement)[44]. Under Article 20 (a) of UCP 600[45], the bill of lading must have significant appearance.

The issuance of a bill of lading could be one original or a full set. If the bill of lading is issued in a set, a such set must contain two original bills or three original bills in common. The number of the bills could be illustrated as 2/2 or 3/3. In case there is only one original, it is expressed as 1/1. The letter of credit requires a full set must be presented, which means all original documents must be presented (Tóth, 2006, p. 70).

5.2.2. Non-negotiable Sea Waybills

The sea waybills are not a document of title and are not negotiable. Hence, they need not be presented at the port to take the delivered goods. Unlike the situation of the bill of lading where the products will be delivered upon the presentation of the documents in case a sea waybill is included in the documents, a person who has his name described in the document shall receive their goods by proving his identity.

The sea waybill is also proof of purchase by the carrier and is evidence for the carrier contract. Normally, the bank will nominate its name as the consignee and the applicant as the party to

[44] The shipper must check the box stating “Consignee” if the bill of lading is negotiable.

[45] Article 20(a) of UCP 600 provides:
“i. indicates the name of the carrier and be signed by:
- the carrier or a named agent for or on behalf of the carrier, or
- the master or a named agent for or on behalf of the master.
Any signature by the carrier, master, or agent must be identified as that of the carrier, master, or agent.
Any signature by an agent must indicate whether the agent has signed for or on behalf of the carrier or for or on behalf of the master.
ii. indicate that the goods have been shipped on board a named vessel at the port of loading stated in the credit by:
- pre-printed wording, or
- an on-board notation indicating the date on which the goods have been shipped on board.
The date of issuance of the bill of lading will be deemed to be the date of shipment unless the bill of lading contains an on-board notation indicating the date of shipment, in which case the date stated in the on board notation will be deemed to be the date of shipment.
If the bill of lading contains the indication "intended vessel" or similar qualification in relation to the name of the vessel, an on-board notation indicating the date of shipment and the name of the actual vessel is required.
iii. indicate shipment from the port of loading to the port of discharge stated in the credit.
If the bill of lading does not indicate the port of loading stated in the credit as the port of loading, or if it contains the indication "intended" or similar qualification in relation to the port of loading, an on-board notation indicating the port of loading as stated in the credit, the date of shipment and the name of the vessel is required. This provision applies even when loading on board or shipment on a named vessel is indicated by pre-printed wording on the bill of lading.
iv. be the sole original bill of lading or, if issued in more than one original, be the full set as indicated on the bill of lading.
v. contains terms and conditions of carriage or makes reference to another source containing the terms and conditions of carriage (short form or blank back bill of lading). Contents of terms and conditions of carriage will not be examined.
vi. contain no indication that it is subject to a charter party.”

be notified to protect the bank's rights. Under Article 21 of UCP 600[46], the non-negotiable sea waybill must have significant appearance:

- "Indicate the name of the carrier" and be signed or authenticated by the carrier or the master or by their named agent.
- "Indicate that the goods have been shipped on board a named vessel at the port of loading stated in the credit".
- "Indicate shipment from the port of loading to the port of discharge stated in the credit";
- "Contain terms and conditions of carriage or make reference to another source containing the terms and conditions of carriage…"
- "Contain no indication that it is subject to a charter party". (International Chamber of Commerce, 2007)

5.2.3. Charter Party Bill of Lading

The phrase "charter party" is the name of the agreement between the vessel's holder and the charterer. In the "charter party" contract, a part or the whole vessel shall be lent to the charter to deliver the cargo to a specific point. The contract will regulate the conditions and responsibilities of each party as well as the freight rate and the payment.

The type of charter has three types:

- Voyage (line) charter: the vessel is hired for single use and is under the owner's control.

[46] Article 21(a) of UCP 600 provides:
"i. indicate the name of the carrier and be signed by:
- the carrier or a named agent for or on behalf of the carrier, or
- the master or a named agent for or on behalf of the master.
Any signature by the carrier, master or agent must be identified as that of the carrier, master or agent.
Any signature by an agent must indicate whether the agent has signed for or on behalf of the carrier or for or on behalf of the master.
ii. indicate that the goods have been shipped on board a named vessel at the port of loading stated in the credit by:
- pre-printed wording, or
- an onboard notation indicating the date on which the goods have been shipped on board.
The date of issuance of the non-negotiable sea waybill will be deemed to be the date of shipment unless the non-negotiable sea waybill contains an onboard notation indicating the date of shipment, in which case the date stated in the onboard notation will be deemed to be the date of shipment.
If the non-negotiable sea waybill contains the indication "intended vessel" or similar qualification in relation to the name of the vessel, an onboard notation indicating the date of shipment and the name of the actual vessel is required.
iii. indicate shipment from the port of loading to the port of discharge stated in the credit.
If the non-negotiable sea waybill does not indicate the port of loading stated in the credit as the port of loading, or if it contains the indication "intended" or similar qualification in relation to the port of loading, an on board notation indicating the port of loading as stated in the credit, the date of shipment and the name of the vessel is required. This provision applies even when loading on board or shipment on a named vessel is indicated by pre-printed wording on the non-negotiable sea waybill.
iv. be the sole original non-negotiable sea waybill or, if issued in more than one original, be the full set as indicated on the non-negotiable sea waybill.
v. contains terms and conditions of carriage or make reference to another source containing the terms and conditions of carriage (short form or blank back non-negotiable sea waybill). Contents of terms and conditions of carriage will not be examined.
vi. contain no indication that it is subject to a charter party."

- Time charter: the shipper hires the boat for a period with a contract and the shipper will operate the ship.
- Demise or Bareboat Charter: the charterer shall have the right to entirely operate the vessel. The full cost of the vessel and legal responsibility will be borne by the charterer.

Under Article 22 of UCP 600[47], the "charter party bill of lading" must appear as:

- It is subjection to a charter party.
- Be signed or authenticated by the owner or their named agent.
- "Indicate that the goods have been shipped on a board a named vessel at the port of loading stated in the credit" (International Chamber of Commerce, 2007).
- "Indicate shipment from the port of loading to the port of discharge stated in the credit" (International Chamber of Commerce, 2007).
- Impressing the vessel is not only propelled by sail.
- Follow the guidance from letters of credit.

5.2.4. Multimodal Transport Documents

Under international commerce, goods are usually transferred over long distances and require more than one kind of transportation and more than one shipping company. Hence, using transport technology including containers allows the goods to be transported from door to door. The containers allow the carrier to transport them from the departing port to their destination port using a chain of transportation without unpacked goods. Chain transportation has proved its effectiveness in proceeding the goods than using several unimodal carriers.

A single transport document used for transferring goods in chain transportation without being interrupted is called a "Multimodal or combined transport document". The first multimodal

[47] Article 22(a) of UCP 600 provides:
"i. be signed by:
- the master or a named agent for or on behalf of the master, or
- the owner or a named agent for or on behalf of the owner, or
- the charterer or a named agent for or on behalf of the charterer.
Any signature by the master, owner, charterer or agent must be identified as that of the master, owner, charterer or agent.
Any signature by an agent must indicate whether the agent has signed for or on behalf of the master, owner or charterer.
An agent signing for or on behalf of the owner or charterer must indicate the name of the owner or charterer .
ii. indicate that the goods have been shipped on board a named vessel at the port of loading stated in the credit by:
- pre-printed wording, or
- an on board notation indicating the date on which the goods have been shipped on board.
The date of issuance of the charter party bill of lading will be deemed to be the date of shipment unless the charter party bill of lading contains an on board notation indicating the date of shipment, in which case the date stated in the on board notation will be deemed to be the date of shipment.
iii. indicate shipment from the port of loading to the port of discharge stated in the credit. The port of discharge may also be shown as a range of ports or a geographical area, as stated in the credit.
iv. be the sole original charter party bill of lading or, if issued in more than one original, be the full set as indicated on the charter party bill of lading."

transport document appeared in the 1960s (UNCTAD Secretariat, 2001)[48] by the International Institute for the Unification of Private Law (hereinafter referred to as "UNIDROIT")[49] and the Comite Maritime International (or "CMI")[50]. The Draft Convention on the International Combined Transport of Goods (known as the "Draft TCM Convention")[51] was prepared by the UNIDROIT but never got used since it received little support.

Because of lacking the international formal documents, using multimodal transportation in international commerce might have some drawbacks because the carriers will use the documents that they think it is suitable. Hence, in 1973, ICC Uniform Rules for a Combined Transport Document was issued (International Chamber of Commerce; UNCITAD, 1973). This rule is revised in 1975 to keep up with the actual practice regarding the delay in the multimodal operator's liability (International Chamber of Commerce; UNCITAD, 1975).

This rule intended to provide some uniformity in documents and gained some achievements such as the COMBIDOC Combined Transport Document issued by BIMCO[52] and FIATA[53] combined Transport Bill of Lading.

The United Nations Convention of International Multimodal Transport of Goods, known as the MT Convention, is outlined in 1980 under the sponsorship of the United Nations but had not widely been accepted (United Nations, 1980). Therefore, the Committee on Shipping of UNCITAD 43 needed to provide provisions for multimodal transport documents. Hence, a new result came out in 1992 as a result based on the Hague Rules and the Hague-Visby Rules, and the existing ICC rules named UNCITAD/ICC Rules for Multimodal Transport Documents (International Chamber of Commerce; UNCITAD, 1992).

The UNCITAD/ICC Rules define the multimodal transport document under Article 2.6 as follows:

> "Multimodal transport document (MT document) means a document evidencing a multimodal transport contract and which can be replaced by electronic data interchange messages insofar as permitted by applicable law and be
>
> (a) Issued in a negotiable form or.
>
> (b) Issued in a non-negotiable form indicating a named consignee." (International Chamber of Commerce; UNCITAD, 1992)

[48] For further information about the Report of the UNCTAD Secretariat on the Implementation of Multimodal Transport Rules, visit https://unctad.org/system/files/official-document/posdtetlbd2.en.pdf.
[49] The UNIDROIT is established in 1926 to prepare modern and appropriate uniform rules for private law. See more at http://www. unidroit.org.
[50] CMI was set up in 1987 and mainly contributes to unify the maritime law. See more at http://www. comitemaritime.org.
[51] The term "TCM" is shorten from the French words "Transport Combiné de Marchandises".
[52] BIMCO is the one of the largest shipping organizations in the world with more than 2500 companies. See more at http://www.bimco.dk.
[53] FIATA is set up in 1926 to represent for over 40 000 logistics firm. See more at http://www.fiata.com.

The legal effect of the UNCITAD/ICC Rules is gained by parties incorporating it into their multimodal transport contract. As a result, the ICC also provides the rules for multimodal or combined transport documents in Article 19 of UCP 600[54] as it must:

- Appear the name of the carrier or his name agent or the master or his named agent.
- "Indicate that the goods have been dispatched, taken in charge or loaded on board at the stated place in the credit" (International Chamber of Commerce, 2007);
- "Indicate the place of dispatch, taking in charge or shipment and the place of final destination stated in the credit" (International Chamber of Commerce, 2007);
- "Contain no indication that it is subject to a charter party" (International Chamber of Commerce, 2007).

Furthermore, Article 19 clearly expresses that "a transport document indicating that transhipment will or may take place is acceptable, even if the credit prohibits transhipment" (International Chamber of Commerce, 2007).

5.2.5. Air Transport Documents

The air transport documents were first introduced in the UCP 500 due to the improvement in transportation and technology. The air transport document performs as a receipt for the carrier as well as proof of the carrier contract just like the bill of lading. However, it is not a document of title.

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[54] Article 19(a) of UCP 600 provides:
"a. A transport document covering at least two different modes of transport (multimodal or combined transport document), however, named, must appear to:
i. indicate the name of the carrier and be signed by:
- the carrier or a named agent for or on behalf of the carrier, or
- the master or a named agent for or on behalf of the master.
Any signature by the carrier, master or agent must be identified as that of the carrier, master or agent.
Any signature by an agent must indicate whether the agent has signed for or on behalf of the carrier or for or on behalf of the master.
ii. indicate that the goods have been dispatched, taken in charge or shipped on board at the place stated in the credit, by:
- pre-printed wording, or
- a stamp or notation indicating the date on which the goods have been dispatched, taken in charge or shipped on board.
The date of issuance of the transport document will be deemed to be the date of dispatch, taking in charge or shipped on board, and the date of shipment. However, if the transport document indicates, by stamp or notation, a date of dispatch, taking in charge or shipped on board, this date will be deemed to be the date of shipment.
iii. indicate the place of dispatch, taking in charge or shipment and the place of final destination stated in the credit, even if:
a. the transport document states, in addition, a different place of dispatch, taking in charge or shipment or place of final destination, or
b. the transport document contains the indication "intended" or similar qualification in relation to the vessel, port of loading or port of discharge.
iv. be the sole original transport document or, if issued in more than one original, be the full set as indicated on the transport document.
v. contain terms and conditions of carriage or make reference to another source containing the terms and conditions of carriage (short form or blank back transport document). Contents of terms and conditions of carriage will not be examined.
vi. contain no indication that it is subject to a charter party."

Under Article 23 of UCP 600[55], the air transport document must:

- Express the name and signature of the carrier, in case the named agent signs the document, he must sign on the side of the carrier.
- Indicate the name of the carrier and be signed, in case the signature belongs to the named agent, he must sign on behalf of the carrier.
- "Indicate for the goods have been accepted for carriage";
- "Indicate the date of issuance";
- "Indicate the airport of departure and the airport of destination";
- "Contain terms and conditions of carriage or make reference to another source containing the terms and conditions of carriage". (International Chamber of Commerce, 2007)

The transhipment shall be allowed once the air transport document indicates it unless the credit expresses the prohibitions. It could be understood that the whole carriage is included in an air transportation paper. The airwaybill is usually issued with three main original copies and nine more copies. The consignor shall sign the first original, and the second and third shall be signed by the carrier. Once the products are accepted for carriage, the third original shall be handed to the consignor or his agent. The third original is enough to present in case the credit requires a full set of originals.

5.2.6. Road, rail, or inland waterway transport documents

Under Article 24 of UCP 600[56], a road, rail, or inland waterway transport document must:

[55] Article 23(a) of UCP 600 provides:
"a. An air transport document, however named, must appear to:
i. indicate the name of the carrier and be signed by:
- the carrier, or
- a named agent for or on behalf of the carrier.
Any signature by the carrier or agent must be identified as that of the carrier or agent.
Any signature by an agent must indicate that the agent has signed for or on behalf of the carrier.
ii. indicate that the goods have been accepted for carriage.
iii. indicate the date of issuance. This date will be deemed to be the date of shipment unless the air transport document contains a specific notation of the actual date of shipment, in which case the date stated in the notation will be deemed to be the date of shipment.
Any other information appearing on the air transport document relative to the flight number and date will not be considered in determining the date of shipment.
iv. indicate the airport of departure and the airport of destination stated in the credit.
v. be the original for consignor or shipper, even if the credit stipulates a full set of originals.
vi. contain terms and conditions of carriage or make reference to another source containing the terms and conditions of carriage. Contents of terms and conditions of carriage will not be examined."

[56] Article 24(a) of UCP 600 provides:
"a. A road, rail or inland waterway transport document, however named, must appear to:
i. indicate the name of the carrier and:
- be signed by the carrier or a named agent for or on behalf of the carrier, or
- indicate receipt of the goods by signature, stamp or notation by the carrier or a named agent for or on behalf of the carrier.
Any signature, stamp or notation of receipt of the goods by the carrier or agent must be identified as that of the carrier or agent.

- Express the carrier's name and be signed or authenticated by the agent on the side of the carrier.
- has "any signature, stamp or notation of receipt" on its face or has wording indicating this effect.
- "Indicate the date of shipment" and the destination.

The road, rail, or inland waterway transport documents work as a certificate and proof of contract, but it is still not a document of title.

5.2.7. Courier and Post Receipts[57]

The transport document released by the courier is called the courier receipt and the receipt issued by the post office is known as the post receipt (or "postal receipt") when the post office is responsible for carrying the goods.

Under Article 25 of UCP 600[58], it is regulated that:

- There must be a stamp on the face of the post receipt, or it must be authenticated and dated from which the Credit stated the goods must be carried.
- The name of the courier must be appeared on the face of the courier certificate to demonstrate the delivery. Moreover, the courier must stamp, sign, or authenticate the transport document. The pick-up date also must be included.

5.2.8. "Clean" Transport Documents

A clean transport document means that the document appears on the face without clauses or remarks observing the "defective nature of the goods and/or the packaging" (International Chamber of Commerce, 2007). According to Article 27 of UCP 600[59], the transportation

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Any signature, stamp or notation of receipt of the goods by the agent must indicate that the agent has signed or acted for or on behalf of the carrier.
If a rail transport document does not identify the carrier, any signature or stamp of the railway company will be accepted as evidence of the document being signed by the carrier.
ii. indicate the date of shipment or the date the goods have been received for shipment, dispatch or carriage at the place stated in the credit. Unless the transport document contains a dated reception stamp, an indication of the date of receipt or a date of shipment, the date of issuance of the transport document will be deemed to be the date of shipment.
iii. indicate the place of shipment and the place of destination stated in the credit."

[57] For further information about FIATA, visit http://www.fiata.com.

[58] Article 25(a) of UCP 600 provides:
"a. A courier receipt, however named, evidencing receipt of goods for transport, must appear to:
i. indicate the name of the courier service and be stamped or signed by the named courier service at the place from which the credit states the goods are to be shipped; and
ii. indicate a date of pick-up or of receipt or wording to this effect. This date will be deemed to be the date of shipment."

[59] Article 27 of UCP 600 provides:
"A bank will only accept a clean transport document. A clean transport document is one bearing no clause or notation expressly declaring a defective condition of the goods or their packaging. The word "clean" need not

document will record the goods as “in apparent good order and condition” (International Chamber of Commerce, 2007).

From Article 32(c) of UCP 500 (International Chamber of Commerce, 1993), based on the experience that banks only accept the “clean” bill of lading, the ICC had added the statement that the phrase “clean” needed not to appear on the transport paper although the credit stated that the bill of lading must have the title “clean on board”. In the UCP 600, the ICC finally admits the practice and expresses that the bank solely accepts the clean bill of lading without exception (International Chamber of Commerce, 2007).

5.3. The Commercial Invoice

In commercial transactions, the seller claims his payment for the goods as well as the service he supplies from the buyer through an “accounting document”. This “accounting document” is called the commercial invoice (Busto, 1994, p. 65). The commercial invoice shall contain the expense of the described goods for the seller to claim the money from the bank.

Name and address of the buyer

Under Article 18 of UCP 600[60], the identity of the applicant, as well as the beneficiary, must be included in the commercial invoice (International Chamber of Commerce, 2007). In other words, it means that the name of the buyer must be addressed in the invoice. However, these rules will not be applied in the case of transferable credit. According to Article 38 of UCP 600[61], transferable credit means it “may be made available in whole or in part to another beneficiary (“second beneficiary”) at the request of the beneficiary (“first beneficiary”)” (International Chamber of Commerce, 2007).

Description of the goods

Under Article 18(c) of UCP 600, the invoice must describe the goods as follows:

> “The description of the goods, services or performance in a commercial invoice must correspond with that appearing in the credit”. (International Chamber of Commerce, 2007)

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appear on a transport document, even if a credit has a requirement for that transport document to be "clean on board".”

[60] Article 18(a) of UCP 600 provides:
“a. A commercial invoice:
i. must appear to have been issued by the beneficiary (except as provided in article 38);
ii. must be made out in the name of the applicant (except as provided in sub-article 38 (g));
iii. must be made out in the same currency as the credit; and
iv. need not be signed.”

[61] Article 38(a) of UCP 600 provides:
“Transferred credit means a credit that has been made available by the transferring bank to a second beneficiary.”

The word "must correspond" does not intend to require the commercial invoice to follow the credit word by word. It means that the content of the credit should be precisely followed by the commercial invoice to prevent misunderstanding. Otherwise, the documents might be rejected because of the wrongful wording in the commercial invoice.

The case *Kydon Compania Naviera S.A v. National Westminster Bank Ltd. (The Lena)* might illustrate the level of compliance in drafting the content of the commercial invoice (Kydon Compania Naviera S.A v. National Westminster Bank Ltd., 1981). The vessel named Lena originated from Greek was sold to Eurasia Carriers Ltd. by the plaintiff. The parties agreed to conduct the payment through an irrevocable letter of credit stating that:

> "the amount of US $ 953771.00 … available by… drafts on them at sight without recourse for full invoice value… purporting to be 100% value of the Greek flag Motor vessel "Lena", built January 1952 of about 11250 tons gross register 6857 tons net register and about 5790 long tons light displacement "as built", with all equipment outfit and gear belonging to her on board, as per M.O.A [Memorandum of Agreement] dated the 2nd July 1974…" (Kydon Compania Naviera S.A v. National Westminster Bank Ltd., 1981)

The bank refused to pay due to, among other things, the discrepancies in the invoice, such as the invoice did not state the construction year as well as the light displacement tonnage "as built" as required under the letter of credit (Kydon Compania Naviera S.A v. National Westminster Bank Ltd., 1981). The tools and the gears that belonged to the vessel were also not mentioned in the invoice. The commercial invoice compared to the wording of the credit appeared that there were differences between the gross and the net tonnage (Kydon Compania Naviera S.A v. National Westminster Bank Ltd., 1981).

The plaintiff then accused the bank of wrongful rejection of payment, arguing that the certificate needed under the credit was the one stating the vessel above. The plaintiff claimed that it was sufficient for the invoice to state "the vessel Lena certified to be as per the memorandum of agreement dated the 2nd of July 1974" (Kydon Compania Naviera S.A v. National Westminster Bank Ltd., 1981).

Through dismissing the allegation of the plaintiff, the Court held that the "beneficiary must follow the words of the credit, and this is so even where he uses an expression, which, although different from the words of the credit, has, as between buyers and seller, the same meaning as such words." (Kydon Compania Naviera S.A v. National Westminster Bank Ltd., 1981). This case demonstrates an example of expressing the words in the commercial invoice since a small difference might make the documents be rejected.

<u>Quantity of the goods</u>

In case the quantity of the goods is not described in the letter of credit in specific units such as box, set, dozen, or piece, a percentage not over 5% of "the total amount of drawings" which

"does not exceed the amount of the credit" will be accepted as stated in Article 30(b) of UCP 600[62] (International Chamber of Commerce, 2007).

In case the letter of credit expresses the quantity of the goods using the word "about" or "approximately", a percentage not over 10% difference between the quantity of the credit and the quantity of the invoice is accepted (International Chamber of Commerce, 2007). In other words, it means that if the parties fail to indicate the specific amount of the goods and use only "about" or "approximately", the difference percentages between the total of the products in the invoice and the number of goods described in the credit is 10% (maximum or less than that). This ratio shall allow the documents to be accepted without being rejected by the bank (since the bank can deny paying if the amount to pay is higher than the actual amount indicated in the credit (International Chamber of Commerce, 2007).

Signature

Under Article 18 (a) (iv) of UCP 600[63] (International Chamber of Commerce, 2007), it is not necessary to have the signature on a commercial invoice. This provision was first added in the UCP 500 (International Chamber of Commerce, 1993). The Working Group explained that they need to "correct the misconception by some parties that invoices must be signed, whether stipulated in the Credit or not" (Busto, 1993, p. 100).

5.4. Insurance Documents

The insurance documents are often added to the set of documents under the requirements of the documentary credit just in case the goods are destroyed or lost. Under Article 28 (a) UCP 600[64], the insurance is required to be "issued and signed by an insurance company, an

[62] Article 30(b) of UCP 600 provides:
"b. A tolerance not to exceed 5% more or 5% less than the quantity of the goods is allowed, provided the credit does not state the quantity in terms of a stipulated number of packing units or individual items and the total amount of the drawings does not exceed the amount of the credit."
[63] Article 18 (a) of UCP 600 provides:
"a. A commercial invoice:
i. must appear to have been issued by the beneficiary (except as provided in article 38);
ii. must be made out in the name of the applicant (except as provided in sub-article 38 (g));
iii. must be made out in the same currency as the credit; and
iv. need not be signed."
[64] Article 28 of UCP 600 provides:
"a. An insurance document, such as an insurance policy, an insurance certificate, or a declaration under an open cover, must appear to be issued and signed by an insurance company, an underwriter or their agents or their proxies.
Any signature by an agent or proxy must indicate whether the agent or proxy has signed for or on behalf of the insurance company or underwriter.
b. When the insurance document indicates that it has been issued in more than one original, all originals must be presented.
c. Cover notes will not be accepted.
d. An insurance policy is acceptable in lieu of an insurance certificate or a declaration under an open cover.
e. The date of the insurance document must be no later than the date of shipment, unless it appears from the insurance document that the cover is effective from a date not later than the date of shipment.

underwriter or their agents or their proxies." (International Chamber of Commerce, 2007). In case the insurance documents are issued in more than one original, the presenter must submit all the originals to the bank as stated in Article 28(b) of UCP 600 (International Chamber of Commerce, 2007). Considering Article 28(c) of UCP 600, the cover notes, which are analysis that covers the contents and information of the insurance contract, shall not be accepted (International Chamber of Commerce, 2007). However, it is acceptable to include an insurance policy with "an open cover" in the submitted documents to the bank (International Chamber of Commerce, 2007)[65].

Article 28 (f)(i) of UCP 600 requires that the "amount of insurance coverage" must be included in the insurance document (International Chamber of Commerce, 2007). In case the credit does not express the percentage of insurance coverage, according to Article 28(f)(ii), it is recommended that "the amount of insurance coverage must be at least 110% of the CIF or CIP value of the goods." (International Chamber of Commerce, 2007). However, if the value of C.I.F[66] or C.I.P[67] is not terminable, the total insurance shall be "calculated on the basis of the amount for which honour or negotiation is requested or the gross value of the goods as shown on the invoice, whichever is greater" (International Chamber of Commerce, 2007).

According to Article 28(g) of UCP 600[68], it is recommended that the insurance documents must express what type of risks are covered (International Chamber of Commerce, 2007). Once

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f.
i.The insurance document must indicate the amount of insurance coverage and be in the same currency as the credit.
ii. A requirement in the credit for insurance coverage to be for a percentage of the value of the goods, of the invoice value or similar is deemed to be the minimum amount of coverage required.
If there is no indication in the credit of the insurance coverage required, the amount of insurance coverage must be at least 110% of the CIF or CIP value of the goods.
When the CIF or CIP value cannot be determined from the documents, the amount of insurance coverage must be calculated on the basis of the amount for which honour or negotiation is requested or the gross value of the goods as shown on the invoice, whichever is greater.
iii. The insurance document must indicate that risks are covered at least between the place of taking in charge or shipment and the place of discharge or final destination as stated in the credit.
g. A credit should state the type of insurance required and, if any, the additional risks to be covered. An insurance document will be accepted without regard to any risks that are not covered if the credit uses imprecise terms such as "usual risks" or "customary risks".
h. When a credit requires insurance against "all risks" and an insurance document is presented containing any "all risks" notation or clause, whether or not bearing the heading "all risks", the insurance document will be accepted without regard to any risks stated to be excluded.
i. An insurance document may contain reference to any exclusion clause.
j. An insurance document may indicate that the cover is subject to a franchise or excess (deductible). "

[65] The open cover is mostly favor by the companies which make commonly shipments because the open cover shall implement coverage for all the cargo which is shipped in the policy period. For further information https://www.investopedia.com/terms/o/open-cover.asp.

[66] C.I.F. is defined in the INCOTERMS which is cost- insurance- freight. Once parties define the CIF term, it means that the seller must bear the costs, the freight as well as the marine insurance to carry the products to the destinated port. See more INCOTERMS 2020 at https://iccwbo.org/resources-for-business/incoterms-rules/incoterms-2020/.

[67] C.I.P stands for Carriage, Insurance Paid to. See more INCOTERMS 2020 at https://iccwbo.org/resources-for-business/incoterms-rules/incoterms-2020/.

[68] Article 28 (g) of UCP 600 provides:

the insurance document uses the term “usual risks” or “customary risks”, the bank shall take the document “without regard to any risks stated to be excluded” (International Chamber of Commerce, 2007).

5.5. Other Documents

Since the UCP is drafted to cover the main documents needed for international transactions, there are some types of documents that might be included in the credits which are not listed in the UCP 600. These extra documents are required by the applicant to guarantee that the beneficiary will perform his obligations in transactions[69]. There might be extra documents as follows:

- Certificate of origin.
- Country of origin.
- Weight certificate[70].

“g. A credit should state the type of insurance required and, if any, the additional risks to be covered. An insurance document will be accepted without regard to any risks that are not covered if the credit uses imprecise terms such as "usual risks" or "customary risks".”

[69] Since the UCP 400, the UCP is applied for both standby letters of credit and commercial letters of credit. Hence, the UCP does not list the “other documents” because the documents which are used in the commercial credits might not be used in standbys. Such a list of documents is unnecessary.

[70] Article 38 of UCP 600 provides:

“If a Credit calls for an attestation or certification of weight in the case of transport other than by sea, banks will accept a weight stamp or declaration of weight which appears to have been superimposed on the transport document by the carrier or his agent unless the Credit specifically stipulates that the attestation or certification of weight must be by means of a separate document.”

CHAPTER VI

THE FOUNDATION PRINCIPLES OF LETTERS OF CREDIT

The commercial utility of the documentary credits is remained due to two essential principles: the Independent Principle and the Strict Compliance Principle.

6.1. The Independent Principle

6.1.1. The Outline

International commerce always has higher risks than domestic business. It is very risky for the seller to ship the goods before receiving money or the buyer might face the possibility of losing money if he pays before the goods land at the arriving port and the seller does not send the goods. Due to the unreliability between parties, documentary credits are created by merchants. The documentary credits remove the risk of not being paid to the seller as well as make sure the buyer does not have to pay money until a set of documents whose title demonstrates the ownership of the cargo is presented to the third party- the bank. Due to the unique character of letters of credit, international commerce runs smoothly. Under the point of view of the England judges, they considered letters of credit as "the lifeblood of international commerce" (RD Harbottle (Mercantile) Ltd v National Westminster Bank Ltd, 1978) (United City Merchants Investments Ltd. v. Royal Bank of Canada, 1981). Hence, the stability of letters of credit might be collapsed if the process of letters of credit is interrupted by unscrupulous parties.

The independent principle is a creation of the financial banking industry to assure the progress of the letter-of-credit transactions runs smoothly. The independent principle (or "the autonomy principle") is believed to be the core of letters of credit. According to this principle, the commitment of the bank to pay for the beneficiary in letters of credit is separated and is independent of the sales contract between the seller and the buyer and the reimbursement contract between the issuer and the applicant. The issuing bank must honour the documents even though there are problems or conflicts raising from the sales contract between seller and buyer (Howard, 1984, p. 957).

The independent principle is expressed in Article 5 of UCP 600 as follows: "Banks deal with documents and not with goods, services or performance to which the documents may relate" (International Chamber of Commerce, 2007). Following this provision, bank issuers must focus on the documents; goods and services are not included in the scope of issuing banks. This principle is also explained more in Article 34 as follows:

> "A bank assumes no liability or responsibility for the form, sufficiency, accuracy, genuineness, falsification or legal effect of any document, or for the general or particular conditions stipulated in a document or superimposed thereon; nor does it assume any liability or responsibility for the description, quantity, weight, quality,

> condition, packing, delivery, value or existence of the goods, services or other performance represented by any document, or for the good faith or acts or omissions, solvency, performance or standing of the consignor, the carrier, the forwarder, the consignee or the insurer of the goods or any other person." (International Chamber of Commerce, 2007)

Article 4 also points out that the banks are separate from the other contracts of letters of credit "Banks are in no way concerned with or bound by such contract, even if any reference whatsoever to it is included in the credit." (International Chamber of Commerce, 2007). Accordingly, the only concern of the issuer is evaluating whether the documents submitted by the beneficiary meet the requirements specified in letters of credit. This also means that only when the beneficiary fails to submit the documents required in letters of credit, then the issuer has the right to refuse to pay. Otherwise, the issuer must pay the beneficiary even if there is a breach of warranty is raised from the underlying contract, the applicant goes bankrupt, or even in the worst scenario, the underlying contract is cancelled, the bank still has to pay the beneficiary if he submits the facially conforming documents (Ellinger, E.P., 1970, pp. 186-188). To some commentators, the independence principle in letters of credit is expressed via the payment liability of the issuing bank (Flint, 2019, p. 372).

6.1.2. The Independent Principle is illustrated in cases of law

In the most famous case law in the documentary credit field, *Sztejn v. Henry Schroeder Banking Corporation* (Sztejn v. Henry Schroder Banking Corp. , 1941), Justice Shientag declared that "a letter of credit is independent of the primary contract of sale between the buyer and the seller." (Sztejn v. Henry Schroder Banking Corp. , 1941). His Honour went further to implicate that "[t]he issuing bank agrees to pay upon presentation of documents, not goods." (Sztejn v. Henry Schroder Banking Corp. , 1941). In another case, the *Westpac Banking Corporation v. South Carolina National Bank*, the Council stated that the bank's sole concern was "the form of the documents presented to it, and not with the underlying facts." (Westpac Banking Corporation v. South Carolina National Bank, 1986). When the bank performed its payment duties, "the underlying facts … forms no part of the bank's function" (Westpac Banking Corporation v. South Carolina National Bank, 1986).

Letters of credit remain their economic capacity by keeping parties in letters of credit within their "zone of expertise" and this is also a part of the independence principle (McLaughlin, 2002, p. 522). The independent principle is a product of merchants' customs just like the letter of credit. Among the aforesaid three main transactions, the bank plays an important role in the second and third transactions and they are experts in the banking business, not in the industry of the merchant (Xiang & Buckley, 2003, p. 121). Hence, the issuers usually deal with paper examinations and payment problems, not the quality of the goods (McLaughlin, 2002, pp. 522-523). In favour of the interest of the applicant, the banks shall draft the letter of credit to assure that their customer (the applicant) might pay against the documents which represent the full performance of the beneficiary.

Bank issuers cannot deal with the services or goods, and the letter of credit must be a "paper-driven device whose operation must turn upon what appears on the face of the paper, not upon circumstances outside them" (Xiang & Buckley, 2003, p. 121). Examining the documents is to check whether the tendered documents comply with the requirements in the letter of credit; however, issuers cannot investigate the facts beyond the submitted documents (Xiang & Buckley, 2003, p. 121). On the contrary, the seller and the buyer usually deal with the consequences of the quality and quantity of the products, sometimes even the shipping of the goods (McLaughlin, 2002, p. 523). Therefore, when the bank issuer in the third contract is put into a position to handle the problems from the underlying contract, they will be out of their "zone of expertise" (McLaughlin, 2002, p. 523) and the commercial usage of the letter of credit will collapse (Xiang & Buckley, 2003, p. 121). Due to the independent principle, the banks will pay against the submission of complied documents despite the situation of the applicant, such as bankruptcy or the cancellation of a sales agreement.

The bank's payment duty is fully protected by the autonomous principle. Lord Diplock in the case *United City Merchants (Investments) Ltd. v. Royal Bank of Canada* had stated:

> "If, on their face, the documents presented to the confirming bank by the seller conform with the requirements of the credit as notified to him by the confirming bank, the bank is under a contractual obligation to the seller to honour the credit, notwithstanding that the bank has knowledge that the seller at the time of presentation of the conforming documents is alleged by the buyer to have, and in fact has already, committed a breach of his contract with the buyer for the sale of the goods to which the documents appear on their face to relate, that would have entitled the buyer to treat the contract of sale as rescinded and to reject the goods and refuse to pay the seller the purchase price. The whole commercial purpose for which the system of confirmed irrevocable documentary credits has been developed in international trade is to give the seller an assured right to be paid before he parts with control of the goods that do not permit any dispute with the buyer as to the performance of the contract of sale being used as a ground for non-payment or reduction or deferment of payment." (United City Merchants Investments Ltd. v. Royal Bank of Canada, 1982)

The only exceptions to restrain the process of letters of credit are the fraud exception and the case of illegality.[71]

6.2. Strict Compliance Principle

6.2.1. The Outline

'There is no room for documents which are almost the same, or which will do just as well'. This statement expresses the point of view of Viscount Summer and the courts in the general (Equitable Trust Co. of New York v. Dawson Partners, Ltd., 1927) about the strict compliance

[71] See Chapter VII for further information about the case of illegality.

principle. According to this principle in Article 14(a) of UCP 600, the document examiners of the bank will check and revise such documents as are submitted to determine whether these documents comply 'on their face' with the requirements defined according to the letter of credit ((International Chamber of Commerce, 2007). If the documents meet the requirements, the bank will honour them, otherwise not (Dolan, 1985, p. 20). The bank is under no duty to look beyond the presented documents (Dolan, 1985, p. 20). This principle is supported by Article 5 of UCC (Uniform of Commercial Code, 1995) and the UCP (International Chamber of Commerce, 2007).

Under the strict compliance principle in light of Article 14, Article 15 and Article 16 of UCP 600, the bank clearly understands that it must check the documents regarding whether they comply on their face with the requirements of the letter (International Chamber of Commerce, 2007) and will not be responsible for any lack of awareness regarding the trade performance of the agreement. Article 4 of UCP also stresses that such credit is autonomous from the sales agreement in which the letter is formed (International Chamber of Commerce, 2007). In this process, the text in the submitted documents is treated like "a mere combination of letters" (Grassi, 1995, p. 112) without any meanings. A document is accepted only if it contains the same words as required under the letter of credit; this practice demands no interpretation and expects the words in the documents to be similar (Grassi, 1995, p. 112). Only the strict 'word to word' method is accepted in relation to the letters of credit (Equitable Trust Co. of New York v. Dawson Partners, Ltd., 1927). Even though this approach has been proven to be too severe, and the beneficiary might think it is too unfair (Dolan, 1996, p. 6.04), it balances between security for parties and the efficiency of letters of credit (Dolan, 1996, p. 603).

The strict compliance principle requires the beneficiary to submit the complying documents and the bank to fulfil its payment obligation once the presented documents conform to the standards in the letter of credit (Dolan, 1985, pp. 21-22). The buyer needs to precisely specify what kinds of documents he needs to prove his possession of the goods from the seller (Grassi, 1995, pp. 112-113). This negotiation between parties does not involve the bank and puts the applicant in a strong position since the beneficiary might find himself stuck in a situation in which he must submit unavailable documents or accepts non-documentary conditions if he does not pay attention to the requirements defined in the letter of credit (Grassi, 1995, p. 113). However, the bank's customer – the buyer – also needs to be well prepared since he will pay for goods that he is unable to examine before the money is transferred (Grassi, 1995, p. 113).

According to the strict compliance principle, the agreement between the parties may not be restructured (Grassi, 1995, p. 113). The beneficiary cannot even argue that he cannot fulfil his duty in the letter of credit because one of the documents that he needs to submit to the bank must be taken from the buyer since the beneficiary has accepted such a requirement under the letter of credit (Grassi, 1995, p. 113) Once the beneficiary accepts the terms, they should follow them. The beneficiary is 'trapped' with the deal since "it is black letter law that the terms and conditions of a letter of credit must be strictly adhered to" (Corporacion De Mercadeo Agricola v. Mellon Bank Int'l, 1979).

6.2.2. The Strict Compliance Principle is illustrated in cases of law

The courts have supported this principle for years and their orientation is clearly stated through cases. The strict compliance rule is clearly illustrated in one of the most famous cases, *Equitable Trust Co. of New York v. Dawson Partners*. The case was about vanilla purchasing between the plaintiff and a seller from Batavia (now known as Jakarta, Indonesia) (Equitable Trust Co. of New York v. Dawson Partners, Ltd., 1927). Parties agreed to process the payment with a letter of credit against the documents including a certificate issued "by experts who are sworn brokers" (Equitable Trust Co. of New York v. Dawson Partners, Ltd., 1927). The seller, nonetheless, submitted the document stating "by an expert who is sworn broker" under the advice of the advising bank (Equitable Trust Co. of New York v. Dawson Partners, Ltd., 1927). The seller was then found to have fraudulent activities toward the buyer and most of the goods turned out rubbish. The holding of the House of Lords expressed their opinions which were the reimbursement obligation of the buyer need not be performed due to "a certificate of quality to be issued by experts- has not been complied with" (Equitable Trust Co. of New York v. Dawson Partners, Ltd., 1927).

Another famous case is *J.H. Rayner & Co. Ltd. v. Hambros's Bank Ltd*. In this case, the parties traded groundnuts and agreed to carry out the payment by an irrevocable letter of credit. The bill of lading submitted by the plaintiff had the wording "machine-shelled groundnut kernels" and "C.R.S" (J.H. Rayner & Co. Ltd. v. Hambros's Bank Ltd, 1942) in the margin which was usually known as shortening phrase for "Coromandel" in commercial practice. These differences were the reason for the rejection from the bank.

The Appeal Court held that the defendant was entitled to refuse the documents because the documents presented did not conform to the requirements under the credit. Justice Goddard stated that since the bank knew the transaction, it must perform its payment obligation against the documents containing the terms in a particular way (J.H. Rayner & Co. Ltd. v. Hambros's Bank Ltd, 1942).

In some other situations, the courts had shown their other point of view in compliance with the strict compliance rule. This principle might be shaped to make it more sensible to the cases. For example, in the case of *All American Semiconductor Inc. v. Wells Fargo Bank, Minnesota N.A*, the bank rejected to pay against the documents submitted because the statement of the beneficiary only contained the name of the company as "All American" instead of the full name, and the invoices stated the name of the company as "All American Semiconductor Inc." (All American Semiconductor Inc. v. Wells Fargo Bank, Minnesota N.A, 2004). The court had expressed that the whole presentation of the documents had precisely described the identity of the beneficiary, hence, the submission was considered complying with the requirements in the letter of credit (All American Semiconductor Inc. v. Wells Fargo Bank, Minnesota N.A, 2004).

In the case, *Carter Petroleum Products Inc. v. Brotherhood Bank and Trust Co.*, the applicant's name in the letter of credit was "Highway 210, LLC". However, the beneficiary presented the draft which stated the applicant's name was "Highway 210 Texaco Travel Plaza, LLC" (Carter

Petroleum Products Inc. v. Brotherhood Bank and Trust Co., 2004). The draft was refused by the bank because it did not" strictly comply" with the stipulated terms in the letter of credit. Such reason then was rejected by the Court, the Court expressed that the draft "did contain all the necessary information requested by the letter of credit. … Moreover, the bank could not have been misled by the nonconformity." (Carter Petroleum Products Inc. v. Brotherhood Bank and Trust Co., 2004).

6.3. The Duty of the Banks in Examining the Presented Documents

Article 14 of UCP 600 has stated the duty of the banks in checking the tendered documents under letters of credit as follows:

> "A nominated bank acting on its nomination, a confirming bank, if any, and the issuing bank must examine a presentation to determine, on the basis of the documents alone, whether or not the documents appear on their face to constitute a complying presentation." (International Chamber of Commerce, 2007)

"On their face"

The ICC emphasizes the term "on their face" as follows:

> "…the decision […] is based exclusively upon the banker's examination of the document, and not upon someone else's understanding…. The phrase "on their face" is not to be interpreted as meaning either the "face" or the "reverse" of the document." (Busto, 1993, p. 39).

ICC also stresses that the bank shall not look over the presented document in Article 34 of UCP 600[72].

"Non-documentary requirements"

Article 14(h) of UCP 600[73] has also clearly stated the non-documentary condition. It could be seen that the ICC has suggested that the bank should ignore and disregard the non-documentary conditions. Sir John Donaldson has also expressed his opinion relating to the non-documentary condition under the letter of credit as follows:

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[72] Article 34 of UCP 600 provides:
"A bank assumes no liability or responsibility for the form, sufficiency, accuracy, genuineness, falsification or legal effect of any document, or for the general or particular conditions stipulated in a document or superimposed thereon; nor does it assume any liability or responsibility for the description, quantity, weight, quality, condition, packing, delivery, value or existence of the goods, services or other performance represented by any document, or for the good faith or acts or omissions, solvency, performance or standing of the consignor, the carrier, the forwarder, the consignee or the insurer of the goods or any other person."

[73] Article 14(h) of UCP 600 provides:
"h. If a credit contains a condition without stipulating the document to indicate compliance with the condition, banks will deem such condition as not stated and will disregard it."

> "This is an unfortunate condition to include in a documentary credit because it breaks the first rule of such a transaction, namely, that the parties are dealing in documents, not facts. The condition required a state of fact to exist." (Banque de l'Indochine et de Suez SA v. JH Rayner (Mincing Lane) Ltd., 1983)

"Time to examine the documents"

Under Article 14(b) of UCP 600, the banks have a maximum of "five banking days" to review the documents presented to them[74] (International Chamber of Commerce, 2007). The previous version, Article 13 of UCP 500, had given the banks up to seven banking days (International Chamber of Commerce, 1993) but the ICC reduces it to five days in UCP 600 (International Chamber of Commerce, 2007).

Having five banking days to investigate does not mean the bank has to use all five banking days to decide the conformity of the documents. The time to determine the compliance of the documents shall be decided based on each case due to several reasons such as the type of transaction, the number of documents presented, etc.

"Discrepancies"

Article 14(d) of UCP 600[75] has standards for the bank in examining the documents, which is the banks must rely on international practice to decide whether the documents have discrepancies. To make international practice clearer, the ICC drafted the ISBP (International Standard Banking Practice for the Examination of Documents under Documentary Letters of Credit) in 2002. It is suggested that the "certain abbreviation" or "obvious misspelling" or mistake in typing should not be considered a discrepancy (International Chamber of Commerce, 2002)[76].

[74] Article 14(b) of UCP 600 provides:
"b. A nominated bank acting on its nomination, a confirming bank, if any, and the issuing bank shall each have a maximum of five banking days following the day of presentation to determine if a presentation is complying. This period is not curtailed or otherwise affected by the occurrence on or after the date of presentation of any expiry date or last day for presentation."
[75] Article 14(d) of UCP 600 provides:
"d. Data in a document, when read in context with the credit, the document itself and international standard banking practice, need not be identical to, but must not conflict with, data in that document, any other stipulated document or the credit."
[76] See more at the Paragraph 6 and 8 of ISBP.

CHAPTER VII

THE FRAUD EXCEPTION

As was mentioned in the previous Chapter, the rule that is considered the main milestone of letters of credit is the independent principle. This rule separates the sales transaction and the contract to open the credit between the issuing bank and the applicant. Hence, the bank does not engage in any controversies arising from the underlying contract. However, the independent principle has its exceptions which as the exception of fraud. The so-called exception of fraud which is known as “fraud rules” will be disclosed in this Chapter.

The process of letters of credit is stable but it will be shattered once fraud is found. The process of letters of credit could be stopped by the courts because of fraud, the obligations of the banks shall be affected; and as a result, such a situation creates several debates and turns fraud rule into the “most controversial and confusing area” (Herbert A. Getz, 1980). Different jurisdiction procedures in some countries regarding fraud rules will be presented in this chapter to give a comprehensive analysis.

As we may be aware, fraud can come in several shapes, and anyone could be a fraudster. Fraud could be present by the buyer and the seller or the third party cooperating to defraud the bank. However, within this Chapter, the author will focus on fraud that comes from the beneficiary.

7.1. The Meaning of Fraud Rules

Fraud is one of the oldest and best-known phenomena in the business world. This popular situation is well-known in international trade, and it should not be encouraged in any situation. The commercial utility of letters of credit will be attacked and so does the public policies (Smith, 1983, p. 96). ICC has stated that "[a]s long as there have been commercial systems in place, there have been those who have tried to manipulate these systems" (International Chamber of Commerce, 1994, p. 9). A volume of litigations is raised at the same time with the increase in using letters of credit (Blodgett & Mayer, 1998) and fraud is the most common reason used by buyers to stop the issuing bank from paying (Leacock, 1984, p. 899). Because of some factors such as the geological distance between the buyer and the seller, the uncertainty in different kinds of payment methods such as payment in advance or cash payment, and the diversity of legal systems, the hazard of fraud should be higher in international trade.

For a long period, the commercial utility of letters of credit has been supported by the independent principle. Article 5 of UCP 600 has declared the obligation of the banks with the independent principle as follows: “Banks deal with documents and not with goods, services or performance to which the documents may relate”. Under this rule, the focus of the bank is the documents, not the goods and the services or facts beyond the documents (International Chamber of Commerce, 2007).

Hence, the bank will not deal with the facts that happened beyond letters of credit, they care about the submitted documents since it is their "zone of expertise" (McLaughlin, 2002, p. 522). The role of the bank has a limitation in its obligation which is checking whether the documents conform to the requirements and then setting up the settlement, not checking the reality behind those papers (ICC International Maritime Bureau, 2002, p. 28). The gap between the reality and the documents is the loophole that unscrupulous parties try to misuse letters of credit (Gao, 2002). The beneficiary is allowed to receive his payment once he submits the conforming documents to the bank and the bank must reimburse even though there are conflicts in the underlying contract. Consequently, if the beneficiary tenders the non-complying documents, the bank has the right to refuse to pay[77] (International Chamber of Commerce, 2007).

Typically, in a case, a forged bill of lading and other fake documents will be submitted by unscrupulous presenters to obtain the payment from the bank. There might be nothing happening behind these forged documents. The buyer will discover the reality when he uses such documents to receive the goods, the goods might not meet the requirements described in the underlying contract, or they could be trash, or in the worst situation, there will be no goods at all. The buyer then brings the case to court, but the seller has already disappeared.

The buyer usually seeks for suitable remedies to block payment in letters of credit when fraud is invoked. However, this action usually put the issuing bank "on the horns of a dilemma" (Dynamics Corp. v. Citizens & Southern National Bank, 1973). The issuer is the buyer's bank and under the irrevocable letters of credit, it must pay the facially complying documents once they are submitted (Schmitthoff, 1980, p. 259). If the buyer is permitted to stop the issuer from accepting the documents due to the non-conforming goods in the underlying contract, the economic benefit of letters of credit will be destroyed (Symons, 1979-1980). Protecting the buyer from fraud but keeping the effectiveness of letters of credit as a commercial instrument is not a simple job (Shaffer v. Brooklyn Park Garden Apt. , 1977).

However, the legislators have not fully understood the position of the banks under letters of credit. From the banks' perspective, generosity, faith, and reputation are extremely important. From the orientation of the banks under the documentary credits, their reputations in international trade are the most important. Lawyers and bankers share different orientations relating to the process of letters of credit. The rationale for the achievement of letters of credit in international trading is the trust between the banks in the banking industry (Davidson, 2003, p. 28).

The interference with the process will destroy the economic benefit of letters of credit. However, allowing the beneficiary receives payment by presenting the forged documents is also unconscionable. By using the mechanism of letters of credit, the bad faith person might

[77] Article 16(a) of UCP 600 provides:
When a nominated bank acting on its nomination, a confirming bank, if any, or the issuing bank determines that a presentation does not comply, it may refuse to honor or negotiate.

take advantage of the "automatic and unstoppable vehicle" (Kozolchyk, 1992, pp. 369-370) and causes losses to other honest parties in the credits.

Lord Diplock had stated:

> "The exception of fraud on the part of the beneficiary seeking to avail himself of the credit is a clear application of the maxim *ex turpi causa non oritur actio* or, if plain English is to be preferred, 'fraud unravels all'. The courts will not allow their process to be used by a dishonest person to carry out the fraud." (United City Merchants Investments Ltd. v. Royal Bank of Canada, 1982)

To deal with fraud in letters of credit, the legislators have created the fraud exception. This provision is mentioned as "an extraordinary rule as it represents a departure from the cardinal principle of the law of letters of credit – the principle of independence. It allows the issuer or a court to view the facts behind the face of conforming documents and to disrupt the payment of a letter of credit when fraud is seen to be involved in the transaction" (Gao, 2002, p. 29)

The fraud exception supports the issuer to examine the facts beyond the presented documents and stop the payment even though the presented documents "on their face" conform to the requirements (Gao, 2002, p. 29). However, the fraud exception still has its own problems. One of the main problems is the fraud standard, which is very hard to define. Such a problem makes the courts hesitate to approach the idea of interfering with the payment process using the fraud rules (Symons, 1979-1980, pp. 345-352). Consequently, the hunting for the standards of fraud leads to the circumstance that courts applied several definitions of fraud to retain its economic advantages (Gao & Buckley, 2003, pp. 298-309). There are some fraud standards which was applied by courts such as "gross", "material", "established", "egregious", "strong and prima facie", "intentional", and "serious" (Gao & Buckley, 2003, pp. 298-309).

The necessary to have fraud rules is urgent, mostly because of three reasons as follows according to Gao and Buckley (2002):

- Loophole closing: the independent principle guarantees to the beneficiaries that they will be paid if they provide the complying documents. However, this principle might lead to a situation where the fraudsters take chances to harm the operation of the documentary credits by tendering the fraudulent documents. The beneficiary might present documents on the face conforming to the conditions in the credits, but in fact, these documents are forged. The banks are expected to stay in their zone, and they also do not have enough knowledge about the underlying contract. The banks need to investigate the documents, not the reality, and they cannot detect actual mistakes beyond the documents (Buckley & Gao, 2002, pp. 664-665).

- Public policies: there is an inconsistency between the law of letters of credit and the public policies of the government in controlling fraud (Byner, 1995, p. 389). For many years, fraudsters and perpetrators have abused the progress of letters of credit and get

benefits thanks to the independent principle by pretending to tender the facially complying documents, and such behaviours make honest merchants hesitate to use the documentary credits (Buckley & Gao, 2002, p. 665).

- Preserve the economic benefit: letters of credit gain their prominence based on the faiths located among sellers, buyers, and banks in the transactions. The sellers and the buyers compromise and put their trust in the third party, the banks, to continue the payment. The fraudsters presenting the forged documents to the banks would lead to several harms to the benefit of various parties in letters of credit. Once the faith between parties fades away, the commerce utility of letters of credit will collapse. To protect the financial advantages of letters of credit as well as faithful merchants, fraud rules must be used (Buckley & Gao, 2002, pp. 666-667).

7.2. Fraud Rules in International Sources

7.2.1. The position of Fraud Rules in the United Nations Convention on Independence Guarantees and Standby Letter of Credit

Fraud rules are described in the UNCITRAL Convention 1995 as follows:

First, in Article 15 of UNCITRAL Convention 1995[78], the Convention brings up the requirements of the submitted documents are the documents presented by the beneficiary must not be in "bad faith" and "none of the elements referred to in subparagraphs (a), (b) and (c) of paragraph 1 of article 19 are present" (UNCITRAL, 1995). This regulation means the progress of the standby or the independence guarantee could be held if the aforementioned elements happened in the tendered documents.

Second, Article 19(1) of UNCITRAL Convention 1995[79] is designed to handle particular circumstances and it harmonizes the interests of the involved parties and gives them the right to against the beneficiary if the documents appeared not "manifest and clear" (UNCITRAL, 1995). This article includes various fact patterns in several legal systems by not using the words "fraud" or "abuse of right" and it tries to avoid multiple definitions or interpretations in case

[78] Article 15 of UNCITRAL Convention 1995 provides that:
"Demand:
(1) Any demand for payment under the undertaking shall be made in a form referred to in paragraph (2) of article 7 and in conformity with the terms and conditions of the undertaking.
(2) Unless otherwise stipulated in the undertaking, the demand and any certification or other document required by the undertaking shall be presented, within the time that a demand for payment may be made to the guarantor/issuer at the place where the undertaking was issued.
(3) The beneficiary, when demanding payment, is deemed to certify that the demand is not in bad faith and that none of the elements referred to in subparagraphs (a), (b) and (c) of paragraph (1) of article 19 are present."

[79] Article 19(1) of UNCITRAL Convention 1995 provides that:
"(1) If it is manifest and clear that:
(a) Any document is not genuine or has been falsified;
(b) No payment is due on the basis asserted in the demand and the supporting documents; or
(c) Judging by the type and purpose of the undertaking, the demand has no conceivable basis, the guarantor/issuer, acting in good faith, has a right, as against the beneficiary, to withhold payment."

law. The fraudulent standard in Article 19(1) is clearly expressed by stating the documents must be obvious without any mistakes or misunderstandings. Moreover, under Article 19(3), the applicants are allowed to ask the courts to grant injunctive relief to suspend the reimbursement once the aforementioned elements under Article 19(1) arise (Davidson, 2010, p. 45).

The fraud rules might be well interpreted in these two situations in the declaration of the Scottish Court of Sessions in *Royal Bank of Scotland v. Holmes*:

> "The authorities disclose two situations in which (the fraud exception) may be relied upon. It may be deployed in support of an application for an interdict to prevent the bank from meeting a demand made by the beneficiary in the letter of credit or guarantee, where the bank's customer is in a position to satisfy the court that there is a prima facie case that the beneficiary is acting fraudulently in making the claim and that the balance of convenience favors interim interdict... The fraud exception may also be deployed as a defence to a claim for reimbursement by the bank against its customer in respect of sums paid in response to the demand of the beneficiary in the letter of credit or guarantee." (Royal Bank of Scotland PLC v. Holmes, 1999)

The UNCITRAL Convention 1995 mainly refers to the rights of the issuer which help them to retain their right to seek reimbursement. The application to open the credit implies that parties must act with good faith, and they should protect the interests of each other. The obligation of the issuing bank in letters of credit is to honour the complying documents when the beneficiary presents them (UNCITRAL, 1995)**.** The issuing bank is irresponsible once the bank still honours the documents even when the bank knows about the fraud and causes loss to the applicant (Davidson, 2010, p. 44).

Under Comment 48 in the Explanatory Note, the UNCITRAL Convention 1995 should be "sensitive to the concern of guarantor/issuers over preserving the commercial reliability of undertakings as promises that are independent of underlying transactions" (UNCITRAL, 1995). Article 19(1) has balanced the interests of competition and considers parties in the credit.

The UNCITRAL Convention 1995 does not nullify any rights of the applicant relating to drafting the terms of the application contract. According to Comment 49, these rights define the non-reimbursement of the buyer once the payment is not properly (UNCITRAL, 1995). In case the applicant brings the case to the court for injunctive relief, Article 19(1) allows the fraud standards to vary based on the courts' opinions and case law.

Third, Article 20 of UNCITRAL Convention 1995[80] presents the standards of proof that courts can refer to once fraud is involved. The application for an injunction can be made if there is

[80] Article 20 of UNCITRAL Convention 1995 provides that:
"Provisional court measures:

strong evidence of fraudulent activities which is described in Article 19(1) and the courts can authorize the principals/applicants to "furnish such form of security" once the principals/applicants seem "suffer serious harm". Furthermore, if there are any criminal purposes involved in the cases, the court could release provisional orders or blocks the payment under Article 20(3).

As has been seen, the UNCITRAL Convention 1995 has inherited the regulations and interpretations relating to the fraud rules over the years from national courts of common law countries as well as national regulations relating to the fraud rules (Buckley & Gao, 2002, p. 710). The UNCITRAL Convention 1995 has illustrated the fraud rules quite clearly. However, the regulations in this Convention still miss some points and can be enhanced more. For example, the UNCITRAL Convention 1995 has not mentioned who could be exempt from the fraud rules or the scope, which is one of the main serious drawbacks of this UNCITRAL Convention 1995. However, the scope of this UNCITRAL Convention 1995 only applies to standby letters of credit and independence guarantees. Even though this thesis mainly focuses on commercial letters of credit, the fraud rules in the UNCITRAL Convention 1995 are noticeable and the author wants to mention them. The UNCITRAL Convention 1995 is not drafted for the commercial letter of credit, so if its scope can be extended, its influence might be bigger (Buckley & Gao, 2002, p. 710).

7.2.2. The position of Fraud Rules in the Uniform of Commerce and Practice for Documentary Credits

The most important set of regulations affecting letters of credit in international trade is the set of private rules depending on the generally accepted customs and practices among bankers and merchants, which is called the Uniform of Commerce and Practice for Documentary Credit. Under Article 5 of UCP 600: "Banks deal with documents and not with goods, services or performance to which the documents may relate". According to this provision, the bank issuers focus mostly on the documents; goods and services are not included. Article 4 also points out that the banks are separate from other contracts as follows "[b]anks are in no way concerned with or bound by such contract, even if any reference whatsoever to it is included in the credit." Accordingly, the only concern of the issuer in letters of credit is evaluating whether the

(1) Where, on an application by the principal/applicant or the instructing party, it is shown that there is a high probability that, with regard to a demand made, or expected to be made, by the beneficiary, one of the circumstances referred to in subparagraphs (a), (b) and (c) of paragraph (1) of article 19 is present, the court, on the basis of immediately available strong evidence, may:
(a) Issue a provisional order to the effect that the beneficiary does not receive payment, including an order that the guarantor/issuer hold the amount of the undertaking, or
(b) Issue a provisional order to the effect that the proceeds of the undertaking paid to the beneficiary are blocked, taking into account whether, in the absence of such an order, the principal/ applicant would be likely to suffer serious harm.
(2) The court, when issuing a provisional order referred to in paragraph (1) of this article, may require the person applying therefor to furnish such form of security as the court deems appropriate.
(3) The court may not issue a provisional order of the kind referred to in paragraph (1) of this article based on any objection to payment other than those referred to in subparagraphs (a), (b) and (c) of paragraph (1) of article 19, or use of the undertaking for a criminal purpose."

documents submitted by the beneficiary meet the requirements stipulated in letters of credit. If the documents meet the requirements stated in the credit, the bank must pay[81].

The independent principle is mentioned in different versions of the UCP, however, the UCP 600 remains silent about the rules of fraud and fraud standards. The ICC Banking Commission has expressed its support for the fraud exception a few times just like in 1995 as follows:

> "There is an exception to these provisions [principle of autonomy and that the bank deals with documents not with goods] in many jurisdictions, namely abuse of rights, or fraud. The ambit of this exception and the ensuing consequences for the beneficiary and/or the nominated bank may differ from one local jurisdiction to another. It is up to the courts to fairly protect the interests of all bona fide parties concerned." (ICC Banking Commission, 1997)

To some scholars like John F. Dolan (1999) or E.P. Ellinger (2004), the UCP must include the fraud exception within its terms. John F. Dolan said "It is important to understand that the Uniform Customs are not law; they are a compilation of what thoughtful bankers feel are good practice, and they fashion what is in the nature of the code of those practices. ...but the idea that they can fashion fraud law or trial procedures in the more than one hundred jurisdictions that recognize the UCP is a fanciful notion." (Dolan, 1999, p. 533); however, some other commentators agree with the silence of the UCP (Kuo, 1995).

The excuse of the ICC for not including the fraud rules in the UCP is that UCP is not a law but a set of customs and practices in international trade. The UCP is considered "rules of best banking practice, not rules for the law" (Goode, 1995, pp. 725-727) and fraud is considered a national problem so if fraud is found in letters of credit then domestic laws should deal with it by granting prohibitions to enjoin the process of letters of credit. However, this point of view has some problems. Even though UCP is not law, it is still recognized and used as "quasi-law in many countries that have little or no statutory law governing letters of credit" (Barnes & Byrne, 1995, pp. 215-216). Indeed, the UCP governs most letters of credit in international trading, which makes the UCP a "de facto law" (Dolan, 1996).

In 2007, UCP 600 is released, which is noted as the latest version, but the ICC remains silent on this problem. In my opinion, the author supports the view of including the fraud exception within the UCP just like the UNCITRAL. Due to the diversifications of the legal systems around the world, it is very frustrating for merchants and even lawyers to follow several rules and codes. The merchants will be more confident in using the UCP as well as the lawyers will

[81] Article 34 of UCP 600 provides:
"A bank assumes no liability or responsibility for the form, sufficiency, accuracy, genuineness, falsification or legal effect of any document, or for the general or particular conditions stipulated in a document or superimposed thereon; nor does it assume any liability or responsibility for the description, quantity, weight, quality, condition, packing, delivery, value or existence of the goods, services or other performance represented by any document, or for the good faith or acts or omissions, solvency, performance or standing of the consignor, the carrier, the forwarder, the consignee or the insurer of the goods or any other person."

have reliable sources of international regulations to believe in. The UCP cannot replace the essential regulations of the national laws; however, having instructions in treating fraudulent activities in letters of credit will allow the courts to keep up with international trade. It could also avoid several problems relating to conflicts by providing sophisticated guidance to international merchants.

7.2.3. Supplement to the Uniform Customs and Practices for Documentary Credit for Electronic Presentation

The Supplement to the Uniform Customs and Practices for Documentary Credit for Electronic Presentation is also known as eUCP. The eUCP is drafted to match the requirements for letters of credit in the electronic trade. The eUCP also remains silent on the fraud rules which is similar to other versions of UCP. However, as James Byrne emphasized "with the additional requirements for authentication of electronic records and today's technology related to digital signatures and message authentication, these [fraud and safety] issues should diminish. … that is not to say that fraud can be eliminated from credit transactions simply by the use of electronic presentation but only that the possibilities for fraud become more limited" (Byrne & Taylor, 2002, p. 18). However, the adoption rate of the eUCP is nearly zero (Cronican, 2013, p. 391). After the eUCP version 1.0 is issued, the percentage of the e-trade business still constitutes less than 1% of the finance field (Godier, 2000). Hence, there might be a chance that the development of technology such as blockchain or smart contracts, as well as the digital signature, can reduce fraud existence (O'Shields, 2017, pp. 181-182) (Larson, 2018, p. 971).

7.3. The position of Fraud Rules in the United Kingdom

7.3.1. Early Case Law in the United Kingdom

Pillans v. Van Mierop

The first case describing the fraud in the letter of credit is recorded in 1765. The case is between *Pillans v. Van Mierop* and it involved problems in the letter of credit, as well as the bill of exchange and the court, and refers to the lex mercatoria. The plaintiffs, Pillans and Rose in Rotterdam, Netherlands, were told by White, a merchant from Ireland, that White wanted to draw on the plaintiffs a sum of 800 pounds (Pillans v. Van Mierop, 1765). Van Mierop and Hopkins in London were asked to issue a credit by White to secure the repayment of the aforesaid amount (Pillans v. Van Mierop, 1765).

Pillans then questioned Van Mierop and Hopkins wanted to see "whether they would accept such bills as they, the plaintiffs, should in about a month's time draw upon the said Van Mierop and Hopkins's house here in London, for 800 pounds upon the credit of White" (Pillans v. Van Mierop, 1765). Van Mierop and Hopkins agreed. Afterwards, when White went broke, Van Mierop and Hopkins noted to the plaintiff not to draw on them. The plaintiff kept insisting to get paid and the defendants refused to set up the settlement. Pillans brought the case to court. The judgment was discussed by Lord Mansfield, Wilmont, and Aston JJ. Within the letter, Van

Mierop and Hopkins had admitted that they shall pay once the plaintiff wanted to draw. Lord Mansfield had expressed his point of view as follows: “All letters of credit relate to future credit; not to debts before incurred; ... A bill cannot be accepted before it is drawn.” (Pillans v. Van Mierop, 1765). At the court, their Honours stated that “Van Mierop and Hopkins were bound by their letter; unless there was some fraud upon them…” (Pillans v. Van Mierop, 1765).

This case was decided more than 250 years ago, however, the point of view of the court was stated straightforwardly which is the court would not tolerate fraudulent manners and the parties are bound by the letters except there is fraud.

Societe Metallurgique v. British Bank for Foreign Trade

There is another case in 1922 which is the *Societe Metallurgique v. British Bank for Foreign Trade*. Societe Metallurgique, the French plaintiff, sold pig iron to Mr Ford, the buyer. Both parties agreed that the letter of credit would be used as a payment method. When the presenter submits the documents including the weight receipt issued by the agent of the buyer in Antwerp as well as the invoice to the British Bank for Foreign Trade, the bank which was the defendant must honour the credit. In the first shipment, the seller presented the documents and received payment. Afterwards, the buyer noticed the defendant for not honouring the second shipment’s documents claiming that the conditions of the pig iron did not match the requirements described in the underlying contract. The buyer received a lot of complaints from his customers who bought the pig irons, so he decided to stop the payment process. Plaintiff decided to bring this case to court claiming that the issuer breached the contract and caused damages. The judges ruled for plaintiff (Societe Metallurgique v. British Bank for Foreign Trade, 1922).

The arguments of the defendant were rejected by Justice Bailhache “There is another case in which the bank would be entitled not to pay, i.e., if the goods were innocently misdescribed in the documents tendered to them- so far misdescribed that the goods might be rejected by the buyers and were so rejected by the buyers. … But here not only am I satisfied that they were not misdescribed, but the buyer has not rejected them but has sold 400 tons of these goods to other buyers.” (Societe Metallurgique v. British Bank for Foreign Trade, 1922). Fraud was not mentioned in this case nor alleged. However, the point of view of the Court was stated clearly that the Court would not stand for any kind of fraud included in the transactions.

United City Merchants Investments Ltd. v. Royal Bank of Canada

One of the most famous cases relating to fraudulent activities in the letter of credit is the case *United City Merchants Investments Ltd. v. Royal Bank of Canada.*

The facts of the case

An English company named Glass Fibers and Equipment Ltd., (hereinafter referred to as “GFE”) entered into a sales contract in October 1975 with Vitrorefuerzos SA (hereinafter referred to as “Vitro”), a Peruvian company to sell glass fibre. Both parties agreed to use the

letter of credit as their payment method; hence, an irrevocable letter of credit was issued by Banco Continental SA in March 1976, and Royal Bank of Canada (hereinafter referred to as "RBC"), the defendant, was the confirmer. The amount of the letter of credit was $ 794,503.20 and the date of shipping from London to Callao, Peru must not be later than 15 December 1976. The London branch of the defendant would pay against the clean bill of lading no later than 31 December 1976 (United City Merchants Investments Ltd. v. Royal Bank of Canada, 1982).

Later, GFE assigned the plaintiff, United City Merchants Investments Ltd., all its entitlements, rights, and benefits through a letter of credit in July 1976. In December of the same year, the preparation of the equipment was done, and it was about to be shipped. The forwarding agent of the seller noticed the details of the conditions of the bill of lading which stated that the deadline of shipping date to ship the products from London to Callao must be before the 15th of December, then the agent forwarded the notices to their loading broker, the American Prudential Lines. The trip of the original vessel was cancelled. Hence, another vessel was used to carry the products which was called the American Accord on the 16th of December 1976. The employer of the freight agency, Mr Baker, without the confirmation of the consignees of the letter of credit and the seller, changed the bill of lading shipping date from 16th of December to 15th of December. The shipping port was stated as the Callao in the bill of lading, meanwhile, the actual depart port was Felixstowe (United City Merchants Investments Ltd. v. Royal Bank of Canada, 1982).

RBC dishonoured the documents claiming that the information in the bills of lading was forged and the commercial invoice did not match the conditions described in the letter of credit. The plaintiff then brought the case to the court for wrongful dishonour, claiming that he was not aware of the wrongful action of Mr Baker and the plaintiff believed that the shipping date, in reality, was the 15th of December (United City Merchants Investments Ltd. v. Royal Bank of Canada, 1982).

The judgment

The decision of the Queens' Bench Division

Justice Mocatta gave the judgment in 1979. He gave judgement for the bank; however, the judgement was not based on the fraud rule. Justice Mocatta also cited the case Sztejn v. Henry Schroder Banking Corp (Sztejn v. Henry Schroder Banking Corp. , 1941) and gave a compelling opinion about the fraud rules. He stated that the obligation to pay the issuer must be fulfilled once the presented documents match the requirements in the letter of credit and the disputes between the parties in the sales contract could not affect the honour of the issuer. However, there was "an exception to the strict rule: the bank ought not to pay under the credit if it knows that the documents are forged or that the request of payment is made fraudulently in circumstances where there is no right to payment" (United City Merchants Investments Ltd. v. Royal Bank of Canada, 1982).

However, Justice Mocatta declared that there is a "vitally different" in this case comparing to Sztejn that is:

> "… although Mr. Baker had acted fraudulently, neither he nor his company were acting on behalf of either of the plaintiffs but were acting as loading brokers on behalf of the American Prudential Lines from whom they received their remuneration… There was no fraud by the plaintiffs nor was there any finding that they knew the date on the bill of lading to be false when they presented the documents..." (United City Merchants Investments Ltd. v. Royal Bank of Canada, 1982).

The judgment of the Court of Appeal

The seller then appealed. The decision of the Queens' Bench Division was reversed by the Court of Appeal based on the fraudulent activity of the third party. The Court of Appeal considered the importance of the independent principle as "the opening of a confirmed letter of credit constitutes a bargain between the banker and the vendor of the goods, which imposes upon the banker an obligation to pay, irrespective of any dispute there may be between the parties as to whether the goods are up to the contract or not. Under a letter of credit, the contract is to buy documents not goods" (United City Merchants Investments Ltd. v. Royal Bank of Canada, 1981, p. 626). The only exception of the independent principle was confirmed again by the Court which was the fraud rules, and the obligations of the bank were confirmed by the Court of Appeal that it should only pay against the legitimate documents. In other words, the bank could be dishonoured if there were forged documents.

Justice Ackner also gave his question in fraud rules whether the fraud rules shall be applied in case the bank had "knowledge" about fraudulent activities (United City Merchants Investments Ltd. v. Royal Bank of Canada, 1981). He then gave his answer by declaring that when the bank was aware that a bill of lading was forged by a third party then the bank should consider it as a non-conforming document "in the same ways as if it knew that the seller was party to the fraud" when the bank knows "a bill of lading has been fraudulently completed by a third party" (United City Merchants Investments Ltd. v. Royal Bank of Canada, 1981). The Court considered that the bank, the purchaser, and the trader together should bear the risks of forged documents performed by a third party.

The House of Lords

The House of Lords reversed the decision of the Court of Appeal by expressing that they agreed with the Trial Court's judgment. Lord Diplock stated:

> "The exception for fraud on the part of the beneficiary seeking to avail himself of the credit is a clear application of the maxim *ex turpi causa non oritur actio*, or if plain English is to be preferred, "fraud unravels all". The courts will not allow their process to be used by a dishonest person to carry out fraud. " (United City Merchants Investments Ltd. v. Royal Bank of Canada, 1982)

Based on hard facts the beneficiary was not conscious of the conduct of Mr Baker when he changed the shipping date and the beneficiary believed the shipping date in the bill of lading "was true and the goods had actually been loaded on or before the 15th of December 1976, as required by the documentary credit" (United City Merchants Investments Ltd. v. Royal Bank of Canada, 1982), the seller was innocent. Concerning the awareness of the beneficiary, the interpretation from Lord Diplock's point of view could be understood as the beneficiary was not in charge of the misstatement since he was not informed about the changes. In another way, the beneficiary would not be responsible for what he did not know. However, if the beneficiary knows about the problems in his documents but still submits them to the bank, regardless of the level of his awareness, the courts should consider it (Ellinger E.P. , 2010, p. 142).

According to Professor Ellinger, he had specified that: "This is likely to require actual knowledge rather than constructive knowledge based on what the beneficiary as a reasonable man should have known. The question of what constitutes actual knowledge should be approached cautiously: a wilful shutting of one's eyes to the truth may in practice lead a court to make a factual finding that the beneficiary did know of the falsity." (Ellinger E.P. , 2010, p. 142). Then, the House of Lords wrapped up that this case had no fraud (United City Merchants Investments Ltd. v. Royal Bank of Canada, 1982).

A critical review of the case

The problem, in this case, is related to the person who commit the fraud. The Trial Court, based on the maxim *ex turpi causa non oritur actio,* had stated that the fraud rules could only be invoked if the person who conducted the wrongful action was the beneficiary. The Appeal Court, on contrary, believed that the nature of the documents was the main problem, not their origin. Hence, the fraud rules must be invoked once there was fraud found in the document regardless of who conducted it. The House of Lords again adopted the maxim *ex turpi causa non oritur actio* and confirmed that the purchaser must pay if the seller had good faith and did not involve in fraudulent activities.

Under the view of the Court of Appeal, the economic benefit of the credit remains thanks to the obligations of the bank to pay for the complied documents and the buyer also promises that the documents presented will be genuine so that the buyer can receive the goods as described in the sales contract. The security of the letter of credit will be threatened if the forged documents are presented and the unscrupulous presenter gets the payment. However, the agreements between the seller and their other parties are beyond the knowledge of the banks, hence, it is nonsense to require the banks to perform their obligations once the presented documents are forged. This conduct creates meaningless security for letters of credit.

Moreover, the obligation of the seller under the credit is tendering the stipulated documents and acting in good faith and "tendering forged documents is thus irrelevant" (Goode, 1980, p. 291). Requiring the bank to honour the documents which the presenter obtains from the third party without knowing the genuineness of the documents is unfair, especially since the

document “has the potential to make fraud by the beneficiary easier to conceal” (Gao, 2002, p. 133). The commercial utility of the letter of credit is to reduce the risks among the parties in the underlying contract, which means the uncertainties between buyer and seller will be lower, not only the risks of the seller will be eliminated. If the tendered documents are not genuine but are still honoured due to the unconscious of the seller in a contract with a third party, the bank will be in danger. The bank must not bear the burden of fraud conducted by the third party. Once the seller claims the wrongful dishonour of the bank, he must know the fraud risk currently stays with the bank. International trade needs specific circumstances under which the obligations of the bank must be conducted if international parties could not work properly (Gao, 2002, pp. 121-135). To wrap up, the identity of the trespasser is not important as the nature of the documents, just like the declaration in the UNCITRAL Convention 1995.

7.3.2. The Fraud Rules in the United Kingdom legislation

The English courts require very high standards for fraud rules. In *Equitable Trust Co. of New York v. Dawson Partners. Ltd*, Lord Sumner had shown his opinion as follows “there is no room for documents which are almost the same, or which will do just as well” (Equitable Trust Co. of New York v. Dawson Partners, Ltd., 1927). This declaration remains the same today.

> “When a letter of credit is issued and confirmed by a bank, the bank must pay it if the documents are in order and the terms of the credit are satisfied. Any dispute between buyer and seller must be settled between themselves. The bank must honour the credit” (Edward Owen Engineering Ltd v Barclays Bank International Ltd, 1978)

The English courts believe that they should not enjoin any payment processes or apply fraud rules in cases where there are no clear frauds involved (Gao & Buckley, 2003, p. 322). The reason behind this narrow approach is that the English courts do not want to create adverse effects on the commerce utility of the letter of credit and violate the independent principle (Alavi, 2015, p. 62).

Normally, the fraud exception in some English cases would be referred to as the documentary fraud (Alavi, 2015, p. 63) and from those decisions, we could understand that the Sztejn case’s standards are only extended to fraud in the documents (Ellinger & Neo, 2010, p. 143). The declaration of Lord Denning MR in the *Edward Owen* case stated that “the request for payment is made fraudulently in circumstances when there is no right to payment” (Edward Owen Engineering Ltd v Barclays Bank International Ltd, 1978).

In Canada, the Supreme Court in *Bank of Nova Scotia v. Angelica- Whitewear Ltd.* also stated that the judgments in the US and those in England were different based on the extension of the fraud rules (Bank of Nova Scotia v. Angelica-Whitewear Ltd., 1987). Under the view of English authorities, the bank must honour the letter of credit, except when the beneficiary submits the fraudulent documents, and the bank is fully conscious of the fraud when it receives the documents. Under the view of the American courts, the fraud rules could be broadened to the sales contract, for example, the goods are completely replaced by trash, but the beneficiary

still submits the facially complying documents for payment. The Supreme Court of Canada shares the same view with the American authorities that the fraud should be expanded to the underlying contract. However, it only extends to the underlying contract fraud where it is "of such a character as to make the demand for payment under the credit a fraudulent one" (Bank of Nova Scotia v. Angelica-Whitewear Ltd., 1987).

A. Requirements to invoke the fraud rules

It appears that the English Courts observe diverse ways in several cases where the applicants bring cases to the courts asking for granting injunctions to stop the banks from honouring the documents presented by the beneficiary (Buckley & Gao, 2002, p. 693). This observation leads to the situation that fraud rules are applied in limited cases (Buckley & Gao, 2002, p. 694) and the standards of fraud are extremely high.

According to English case law, the Courts normally required very strong evidence and a narrow definition of fraud. The fraud rules could be invoked once:

- The fraud must be "clear" or "obvious" to the issuers' knowledge.

The disagreement over the quality of the products shall not be enough to invoke the fraud rules. The fraud rules will be invoked when the contracted products are "so obviously defective that the representation of shipment is plainly false" (Discount Records Ltd. v. Barclays Bank Ltd, 1975). The fraud must be "timely" (ICC International Maritime Bureau, 2002, p. 49) and the beneficiary must be mindful of or be involved in fraudulent activities.

- Clear evidence of fraud

Courts in England have been very hesitant to interfere with the process of the letter of credit and observe truly narrow access against the fraud rules. In *Hamzeh Malas & Sons v. British Imex Industries Ltd.*, Lord Justice Jenkins illustrates that:

> "An elaborate commercial system has been built up on the footing that bankers' confirmed credits are of that character, and, in my judgment, it would be wrong for this court in the present case to interfere with that established practice… that system… would break down completely if a dispute as between the vendor and the purchaser was to have the effect of "freezing"…" (Hamzeh Malas & Sons v. British Imex Industries Ltd., 1957)

As has been mentioned, the fraud rules in England require very high standards since the English courts are afraid of abusing the financial advantages of the letter of credit. These clear standards are proven clearly in the case *Discount Records Ltd. v. Barclays Bank Ltd*. The English plaintiff bought 825 cassettes and 8625 discs from a French company called Promodiscs. A letter of credit was issued in favour of the seller. The seller presented the documents to their confirming bank in Paris after sending the products and getting paid. The buyer, right after receiving the

goods, immediately took their case to the court asking for an injunction to stop the issuer from reimbursing the confirmer. However, Justice Megarry denied the claim of the buyer:

> "…In the present case there is, of course, no established fraud, but merely an allegation of fraud. The defendants, who were not concerned with that matter, have understandably adducted no evidence on the issue of fraud. Indeed, it seems unlikely that any action to which Promodisc was not a party would contain the evidence required to resolve this issue. Accordingly, the matter has to be dealt with on the footing that this is a case in which *fraud is alleged but has not been established.*" (Discount Records Ltd. v. Barclays Bank Ltd, 1975)

Even though the buyer had shown the pieces of evidence to the third party's witness, showing that:

> "…94 cartoons, but of these two were empty, five were filled with rubbish or packing, twenty-five of the records boxes and three of the cassette boxes were only partly filled, and two boxes labelled as cassettes were filled with records; instead of 825 cassettes, as ordered, there were only 518 cassettes and 25 cartridges. Out of the 518 cassettes delivered, 75 per cent were not as ordered… out of the 8,625 recorded ordered, only 275 were delivered as per order." (Discount Records Ltd. v. Barclays Bank Ltd, 1975)

With this evidence, the court still considered that "fraud is alleged but has not been established" (Discount Records Ltd. v. Barclays Bank Ltd, 1975). Under this statement, the involvement of the fraud rules to stop the payment from the bank to the beneficiary is nearly impossible even the confirmation of the Court in *United City Merchants Investments Ltd. v. Royal Bank of Canada* had stated that they "will not allow their process to be used by a dishonest person to carry out a fraud." (United City Merchants Investments Ltd. v. Royal Bank of Canada, 1982). Through this case, the English authority had expressed their fraud standards which were exceedingly high. Even though the buyer inspected the products, the court was not satisfied with the pieces of evidence and considered they were not enough to end the remittance process of the bank. The English court had shown a truly high standard in this case since "it is only in exceptional cases that the courts will interfere with the machinery of irrevocable obligations assumed by banks. [...] Except possibly in clear cases of fraud of which the banks have noticed, the courts will leave the merchants to settle their disputes under the contracts by litigation or arbitration as available to them or stipulated by the contract.[…] Otherwise, trust in international commerce could be irreparably damaged" (RD Harbottle (Mercantil) Ltd v National Westminster Bank Ltd, 1978).

- The bank is aware of the fraud.

To invoke fraud rules in the allegations submitted to the court, the plaintiff must prove that the bank knows about fraud. This point of view was proven in the case *Edward Owen Engineering Ltd., v. Barclays Bank International Ltd.*

> "The only circumstances which would justify the bank not complying with the demand would be those ... if it had been clear and obvious to the bank that the buyers had been guilty of fraud." (Edward Owen Engineering Ltd v Barclays Bank International Ltd, 1978)

The court in the case *Bolivinter Oil SA v. Chase Manhattan Bank* also stated that:

> "The wholly exceptional case where an injunction may be granted is where it is proved that the bank knows that any demand for payment already made, or which may thereafter be made will clearly be fraudulent. But the evidence must be clear, both as to the fact of fraud and as to the bank's knowledge." (Bolivinter Oil SA v. Chase Manhattan Bank NA, 1984)

- The "timely" of the bank's awareness

Within this criterion, the English authority invokes the fraud rules and allows the bank to dishonour the credit in case they know about the fraud "timely" (ICC International Maritime Bureau, 2002, p. 49). In other words, the bank is fully allowed to not honour the credit if it is informed about fraudulent activities committed by the beneficiary at the time of the credit submission or after that but before the remittance day.

The question of "time" is considered in the case *Czarnikow-Rionda Sugar Trading Inc. v. Standard Bank London Limited*. Rionda, the plaintiff, was a sugar trader who had a long-term contract with Brazilian Dine Group, which owns three sugar mills. Since alcohol was a product made from sugar cane, so Rionda had received a pre-finance based on the contract to secure the guarantee of sugar cane and alcohol (Czarnikow-Rionda Sugar Trading Inc v. Standard Bank London Ltd and Others, 1999).

To help the Dine Group overcome the cash flow issue, the plaintiff supported reselling the alcohol of Dine Group in Brazil. The letter of credit was chosen as the payment method and Rionda allowed its name to appear as the applicant in the letter of credit and became the intermediate party. The buyer then opened a back-to-back letter of credit for its supplier which was issued by the Banque Cantonale de Geneve and the United European Bank. These banks later indicated a few inconsistencies in the documents which Rionda had waived, and then these banks accepted the presentation and sought reimbursement at Standard Bank by delivering the documents.

The plaintiff then realized that the sugar cane did not exist and the alcohol they had pledged for was just water, he immediately sought protection and brought the case to court. The plaintiff then received an injunction before the trial court to prevent Standard Bank to reimburse the two banks based on the information that the two Swiss banks had information about the fraud but ignored it (Czarnikow-Rionda Sugar Trading Inc v. Standard Bank London Ltd and Others, 1999).

In the court's opinion related to "timely", the court declared that:

> "The interest in the integrity of banking contracts under which banks made themselves liable on their letters of credit or their guarantees is so great that not even fraud can be allowed to intervene unless the fraud comes to the notice of the bank (a) *in time, i.e. in any event before the beneficiary is paid, and (b) in such a way that it can be said that the bank had knowledge of the fraud*." (Czarnikow-Rionda Sugar Trading Inc v. Standard Bank London Ltd and Others, 1999)

Rionda was not able to summon the fraud rules and stopped the payment process since the two Swiss banks had given the discount before the scam was realized.

- The beneficiary is involved or is noticed in the fraud

The fraud rules shall not be invoked if the presenter is not aware of fraudulent activities and the other parties have conducted the fraud. As in the case *United City Merchants (Investments) Ltd v. Royal Bank of Canada*, the House of Lords had declared that the beneficiary was not informed about the fraud and the third party had conducted the fraud, hence, with good faith, the beneficiary should be paid. This declaration is clearly expressed again through the case *Montrod Ltd. v. Grundkötter Fleischvertriebs GmbH*. The plaintiff, Montrod, acted as an assistant in the trading process by becoming the applicant for the letter of credit which was issued for the agreement between the defendant and the buyer. Montrod was not the buyer, but his name was placed as the applicant in the credit and Montrod did not have any contract with the seller. When the buyer announced to the seller that the inspection certificates should be signed by the seller's employee on behalf of Montrod, the seller believed that he had the right to do so (Montrod Ltd. v. Grundkötter Fleischvertriebs GmbH & Ors, 2001).

The trial court declared that because the seller did not conduct fraudulent activities, the seller deserved the payment. The Appeal Court supported the decision of the Trial Court and expressed that:

> "The fraud exception to the autonomy principle recognized in English law has hitherto been restricted to, and it is in my view desirable that it should remain based upon, the fraud or knowledge of fraud on the part of the beneficiary or other party seeking payment under and in accordance with the terms of the letter of credit. It should not be avoided or extended by the argument that a document presented, which conforms on its face with the terms of the letter of the credit, is nonetheless of a character which disentitles the person making the demand to pay because it is fraudulent in itself, independently of the knowledge and bona fides of the demanding party. In my view, that is the clear import of Lord Diplock's observations in Gian Singh and in the United City Merchants case, in which all their Lordships concurred." (Montrod Ltd. v. Grundkötter Fleischvertriebs GmbH & Ors, 2001)

The opinion of the English court was clearly shown in this case since they invoked fraud rules only in the circumstance in which the beneficiary must participate in fraudulent activities or know about fraud. Within this view, the identity of the party who commits fraud is the main problem, not the nature of the document. The intention of the beneficiary will be taken into consideration since the court requires the beneficiary that he must know about fraudulent activities. Even if the third-party commits fraud beyond the awareness of the beneficiary or the beneficiary commits fraud by himself without his conscious, the innocence of the beneficiary makes the bank accept the presented documents even though the bank is informed about the fraud.

B. The nullity exception

The Montrod case also showed another problem which is called "nullity". There is a question that bothers the English court when the beneficiary presents a null and void document, but he is not conscious of the nullity, then whether the bank is allowed to dishonour. Or in another way, whether the bank could use the nullity as an excuse for its dishonour of the presented documents to the innocent beneficiary or the bona fide party. According to the case law, the answer is negative.

The nullity problem was early mentioned in the case *United City Merchants (Investments) Ltd, v. Royal Bank of Canada*. Within this case, in His Honour's judgment, Lord Diplock had preserved the question:

> "I would prefer to leave open the question of the rights of an innocent seller beneficiary against the confirming bank when a document presented by him is a nullity because unknown to him that it was forged by some third party, for that question does not arise in the instant case" (United City Merchants Investments Ltd. v. Royal Bank of Canada, 1982).

In 2001, the court in the Montrod case dealt with the nullity exception. Within this case, Lord Justice Potter stated the exception in the following way:

> "The creation of a general nullity exception, the formulation of which does not seem to me susceptible of precision, involves making undesirable inroads into the principles of autonomy and negotiability universally recognized in relation to letter of credit transactions. … If a general nullity exception were to be introduced as part of English law it would place banks in a further dilemma as to the necessity to investigate facts which they are not competent to do and from which UCP 500 is plainly concerned to exempt them. Further such an exception would be likely to act unfairly upon beneficiaries participating in a chain of contracts in cases where their good faith is not in question. Such a development would thus undermine the system of financing international trade by means of documentary credits." (Montrod Ltd. v. Grundkötter Fleischvertriebs GmbH & Ors, 2001)

It has been several debates among commentators about whether the Court of Appeal in this case correctly rejects the nullity exception. For some commentators, the bank's main responsibility is to honour the conforming documents presented to the bank under the credit, not for the documents on the face complying with the requirements. On the other side, Hooley (2003, p. 91) says "a nullity document is a worthless piece of paper" so that the banks will be put in a dangerous position which threatens their chance to seek reimbursement.

The rejection of the nullity exception once again proves that the English court's opinion about enjoining the process of letters of credit is very strict, and the courts hesitate to invoke the fraud rules unless fraud is established by the beneficiary, or the beneficiary is fully aware of the fraud.

C. The fraud standards under the English authority's point of view

One of the standards accepted by English courts is "material representations." (United City Merchants Investments Ltd. v. Royal Bank of Canada, 1982). In this case, the bank turned the documents down based on the ground that the bill of lading was fraudulently pre-dated which was conducted by a third party. Lord Diplock discussed the fraud standards as follows:

> "…where the seller, for the purpose of drawing on the credit, fraudulently presents to the confirming bank documents that contain, expressly or by implication, *material representations* of fact that to his knowledge are untrue." (United City Merchants Investments Ltd. v. Royal Bank of Canada, 1982)

According to His Honour, the fraud exception would be involved once "material representations" fraud happened (Gao & Buckley, 2003, p. 323). As can be seen, the "material" which was brought up in these comments was somehow related to the clarification of the "material fraud" in the Revised Article 5 of UCC. Raymond Jack (1991, p. 118) states the meaning of "material" is "material to the bank duty to pay, so that if the document stated the truth the bank would be obliged to reject the documents". However, this point of view was not similar to the point of Lord Diplock:

> "…material to the price which the goods to which the documents relate would fetch on sale if, failing reimbursement by the buyer, the bank should be driven to realize its security." (United City Merchants Investments Ltd. v. Royal Bank of Canada, 1982)

From His Honour's orientation, the "material misrepresentation" must be related to the goods' value (Gao & Buckley, 2003, p. 323). Therefore, the antedating date in the bill of lading is not "material" because the value of goods is not affected. Jack's explanation could be understood that predating a bill of lading could be recognized as material fraud since the bank could turn the documents down even when the presented bill of lading has the exact date as required in the letter of credit (Jack, 1991). Hence, the observation of Lord Diplock is considered inconsistent, and Jack's interpretation is acknowledged as superior declaration (Gao & Buckley, 2003, p. 323).

7.4. The Fraud Rules position in the United States

7.4.1. Early Cases Law in the United States

Higgins v. Steinhardter

One of the earliest cases related to fraudulent activities in letters of credit in the US is *Higgins v. Steinhardter* happened in 1919 in the US. The plaintiff, Higgins, took legal action to stop the John Monroe Co. (the issuer) from obtaining and reimbursing the documents presented by the defendant. The letter of credit clearly expressed that the shipment of walnut needed to be shipped before 7th November 1918; bills of lading and consular invoice should accompany the documents. The plaintiff accused that the walnuts were not shipped by the defendant from Spain until December 1918 and the plaintiff further claimed that the shipment document was forged by stating the departure date was 30th October 1918. Monroe Co. was notified of the plaintiff's facts, however, the issuer still accepted and paid for the defendant (Higgins v. Steinhardter, 1919). The court noted and granted the injunction stating that the shipment was made after the date cited in the letter of credit, which was contrary to the will of the applicant. Hence, "if the shipment was made subsequent to that date, a payment made against said credit would be unauthorized" (Higgins v. Steinhardter, 1919)

This case happened in the year 1919, the period when letters of credit were shaped into their modern form (Ellinger, 1984, p. 37). The court decided to grant injunctive relief to stop the payment based on the fact that the defendant counterfeited the bill of lading, not on the foundation of the fraud rules. Even the plaintiff made their claims on the fact that there was a false statement related to the shipment's date, not on the foundation of fraudulent activities. The plaintiff sued the defendant for defaulting on the contract, not for fraud (Buckley & Gao, 2002, p. 670). Through this case, it seemed like the fraud rules in the early 20th century in the case related to letters of credit were in their beginning but merchants at that time did not realize it yet. Both the plaintiff and the judge did not refer to the fraud rules, however, "they found another route to meet that end" (Buckley & Gao, 2002, p. 670).

Old Colony Trust Co. v. Lawyers' Title & Trust Co.

There was also a case in the 1920s in which fraud disturbed the payment process. In the case *Old Colony Trust Co. v. Lawyers' Title & Trust Co.,* the plaintiff had sold sugar to a seller. It was announced that the defendant issued a letter of credit in favour of the plaintiff (Old Colony Trust Co. v. Lawyers Title & Trust Co.,, 1924). The letter of credit stated that documents must contain "net landed weight" and be made before November 30, 1920. The negotiable delivery orders and warehouse receipts must be attached along with the documents. The problems were the net landed weight could only be confirmed once the customs weighed the landed goods, and the warehouseman issued the warehouse receipt if only the goods were under his actual possession. The documents were presented to the issuing bank before the expiration day even though the earliest date that the shipments cleared the customs was December 30, 1920. The

documents were rejected by the issuer based on the explanation that the documents did not meet the requests stated in the letter of credit. To recover from the breach of contract of the defendant, the applicant brought the case to court. The court then rejected the claims of the plaintiff (Old Colony Trust Co. v. Lawyers Title & Trust Co.,, 1924). The Second Circuit Court of Appeal maintained the original judgment and noted:

> "Obviously, when the issuer of a letter of credit knows that a document, although correct in form, is, in point of fact, false or illegal, he cannot be called upon to recognize such a document as complying with the terms of a letter of credit." (Old Colony Trust Co. v. Lawyers Title & Trust Co.,, 1924)

In these two early cases, there were some similarities such as fraudulent documents and payments being stopped by the courts due to fraud. However, the main difference between the *Higgins* and the *Old Colony* is the foundation on which the court based to grant their judgments: in *Old Colony*, the court considered that the documents with fraud could not be seen as complying documents while in *Higgins*, the payment was stopped because the court granted an embargo based on the foundation that the information in the bill of lading was considered "unauthorized".

Maurice O'Meara Co. v. National Park Bank of New York

One of the most famous cases years ago is *Maurice O'Meara Co. v. National Park Bank of New York.* A correspondent bank justified its refusal to honour a seller's drafts by claiming that the tensile strength of the newsprint did not match the contracted quality (Maurice O'Meara Co. v. National Park Bank of New York, 1925). Instead of testing whether the *documents* conformed to the requirements in the credit, the bank tested the *goods* to determine whether they followed the instructions from the sales contract. The seller later filed a suit to the Court of Appeals to object to the Court of Trial's judgment, claiming that the obligation of the bank was not checking the quality of the goods but examining the documents. The bank could only check the goods if the letter of credit required them to do so. Once the requirements of the credit were matched, the bank had to pay (Maurice O'Meara Co. v. National Park Bank of New York, 1925). The Court of Appeals of New York then rejected the claim of the issuing bank claiming that they had reasonable doubt about the newsprint paper.

Justice Cardozo's opinion about the case *Maurice O'Meara Co. v. National Park Bank of New York* was expressed as follows:

> The controversy arises between the bank and a seller who has misrepresented the security upon which advances are demanded. Between parties so situated, payment may be resisted if the documents are false." (Maurice O'Meara Co. v. National Park Bank of New York, 1925)

According to Buckley & Gao (2002), the reasons why the case of *Maurice O'Meara* was extremely sophisticated are because: *First*, Justice Cardozo did not only consider the payment

of the false documents should be stopped but also recognized the involvement of the third parties, and the issuer's security interest. *Second*, this case was "both litigated and decided on the basis of the law of letter of credit, and …, handled as a case of contract." (Marine Midland Grace Trust Co. v. Banco del Pais, 1966). *Finally*, the court in *O'Meara* applied the independent principle in explaining the case as well as using the fraud rules.

Intraworld Industries v. Girard Trust Bank

Intraworld Industries Inc v. Girard Trust Bank included a complicated situation where the applicant tried to stop the payment process of the standby letter of credit. The applicant, Intraworld, had joined a leasing contract with a Swiss Hotel and as a lessee, the applicant had required the bank to open a standby letter of credit in favour of the lessor to secure the lease payment. In the standby credit, once the applicant did not pay the rent due as stated under the lease contract, the issuer would accept and pay for the documents including the statement with the signature of the beneficiary (Intraworld Industries v. Girard Trust Bank, 1975).

When the applicant knew that the beneficiary submits the documents claiming that they followed the conditions of the standby after the dispute arose, they tried to stop the payment by invoking the fraud rules and claimed that the documents presented by the beneficiary were fake because the lease was terminated, so that there was no due of rent and the beneficiary was only seeking the stipulated penalty. (Intraworld Industries v. Girard Trust Bank, 1975)

The standard of fraud discussed in this case was cited as follows:

> "[t]he circumstances which will justify an injunction against honor must be narrowly limited to situations of fraud in which the wrongdoing of the beneficiary has so vitiated the entire transaction that the legitimate purposes of the independence of the issuer's obligation would no longer be served." (Intraworld Industries v. Girard Trust Bank, 1975)

The Supreme Court of Pennsylvania found that the allegations against the plaintiff were not true. The leasing contract proved that once the lessee failed to perform their rental payment obligation, the lessor could draw under the standby and terminate the lease contract instantly without any further announcement. The Court then gave its reasons as follows:

> "In light of the basic rule of the independence of the issuer's engagement and the importance of this rule to the effectuation of the purposes of the letter of credit, we think that the circumstances which will justify an injunction against honor must be narrowly limited to situations of fraud in which the wrongdoing of the beneficiary has so vitiated the entire transaction that the legitimate purposes of the independence of the issuer's obligation would no longer be served. A court of equity has limited duty of "guaranteeing that [the beneficiary] not be allowed to take unconscientious advantage of the situation and run off with plaintiff's money on a pro forma declaration which has absolutely no basis in fact". (Intraworld Industries v. Girard Trust Bank, 1975)

The Stzejn case - Sztejn v. Schroder Banking Corp

The landmark case relating to the fraud rules must be the Sztejn case. The judgment of Justice Shientag in the Sztejn case has introduced the guidelines for the fraud rules which were systematized in the Uniform of Commercial Code and are mentioned in several cases concerning fraudulent activities in letters of credit in the common law countries (Buckley & Gao, 2002, p. 676).

Facts

In the *Sztejn v. Schroder Banking Corp*., Chester Charles Sztejn in the United States bought hog bristles originating from India from a company called Transea Traders Ltd., Both parties agreed to conduct the payment by an irrevocable letter of credit. Such documentary credit was issued by Schroder. According to Transea, they had shipped fifty cases of goods on a ship and then received a bill of lading and commercial invoices. In India, Chartered Bank in Cawnpore was chosen to be the correspondent bank to receive and honour the documents presented by Transea if the documents conformed to the requirements from the credit.

Before the payment, Sztejn required the New York court for an order forbidding payment claiming that the submitted documents were forged; the merchant had shipped "cow hair, other worthless material and rubbish" (Sztejn v. Henry Schroder Banking Corp. , 1941). The court then stated that:

> "These documents describe the bristles called for by the letter of credit. However, the complaint alleges that in fact Transea filled the fifty crates with cow hair, other worthless material and rubbish with the intent to simulate genuine merchandise and defraud the plaintiff… the complaint then alleges that Transea drew a draft under the letter of credit to the order of The Chartered Bank and delivered the draft and the fraudulent documents to 'the Chartered Bank at Cawnpore, India, for collection for the account of said defendant Transea." (Sztejn v. Henry Schroder Banking Corp. , 1941)

Critical reviews of the case

For purposes of the hearing court, all the claims by the plaintiff were acknowledged to be true by Justice Shientag which meant Transea had shipped trash and the Chartered Bank could not be considered an innocent holder in due course. The dismission of the Charter Bank about the plaintiff's claims was rejected by Justice Shientag because of the commitment to establishing fraud in the sales contract (Alavi, 2015, p. 55).

From the point of Justice Shientag's view, the independent principle was important, and it was "necessary to preserve the efficiency of the letter of credit as an instrument for the financing of trade" (Sztejn v. Henry Schroder Banking Corp. , 1941). However, it should not be used as a shield to shelter the "unscrupulous seller" even if the documents on their face conform to the

requirements from the letter of credit (Sztejn v. Henry Schroder Banking Corp. , 1941). His Honour also recognized the fraud exception by declaring that the interruption in the payment progress of the letter of credit would be considered "most unfortunate" because it would put pressure on the letter of credit since its main function was to maintain a stable payment for the seller. His Honour also expressed that looking beyond the presented documents must be avoided. Justice Shientag also gave the differences between the mere breach of the warranty in the sales contract and the fraud involved in the letter-of-credit transactions by the beneficiary.

Within this case, there were two other issues discussed:

First, is the interest of the issuing bank. Justice Shientag stated that the fraud might affect the interest of the issuing bank "Although the bank is not interested in the exact detailed performance of the sales contract, it is vitally interested in assuring itself that there are some goods represented by the documents" (Sztejn v. Henry Schroder Banking Corp. , 1941). The court also affirmed that Charter Bank was not an honest holder in due course due to the act of attempting to obtain the payment from the applicant. Hence, the Chartered Bank could be assumed as guilty of "intentional fraud".

Second, the immunity of the holders in due course. His Honour stated that "no hardship will be caused" when banks refused to pay for the documents which were claimed as forged, or in case they were informed about the fraud in the presented documents "in the hand of one who stands in the same position as the fraudulent seller…" (Sztejn v. Henry Schroder Banking Corp. , 1941).

While stating the importance of the independent principle "It is well established that a letter of credit is independent of the primary contract of sale between the buyer and the seller" (Sztejn v. Henry Schroder Banking Corp. , 1941), Justice Shientag also created the foundation principles for the fraud rules as follows:

First, fraud is the only reason to suspend the payment in letters of credit. Breach of warranty does not count as a reason to stop any reimbursements in letters of credit. "For the purpose of this motion the allegations of the complaint must be deemed established … Therefore, it must be assumed that Transea was engaged in a scheme to defraud the plaintiffs …, that the merchandise shipped by Transea is worthless rubbish and that the Chartered Bank is not an innocent holder of the draft for value but is merely attempting to procure payment of the draft for Transea's account" (Sztejn v. Henry Schroder Banking Corp. , 1941).

Second, fraud must be established, and only precise allegations can cause the interruption. The court declared that "It is true that even though the documents are forged or fraudulent, if the issuing bank has already paid the draft before receiving notice of the seller's fraud, it will be protected if it exercised reasonable diligence before making such payment." (Sztejn v. Henry Schroder Banking Corp. , 1941). The explanation of "reasonable diligence" and "notice" could be understood as the "notice" which the issuing bank receives can be the reason for them for

not paying because the issuer has an excuse to believe that fraudulent activity has been established (Sztejn v. Henry Schroder Banking Corp. , 1941).

Third, payment for the holders in due course cannot be stopped even when fraud is claimed.

Compared to the early 20th century cases, even though we must note that all the claims of the plaintiff were assumed to be true, the judgment in the *Sztejn* case by Justice Shientag still makes a big step. In previous cases, fraud rules have never been mentioned or used. In this *Sztejn* case, not only this is the first case that fraud rules were mentioned, Justice Shientag also establishes clear guidelines for future cases relating to fraudulent activities in letters of credit.

7.4.2. The Fraud Rules in the United States legislation

Because the usage of documentary credit in international trading is increasing, some countries had issued specified regulations to govern letters of credit. The United States also has an article in a code to regulate the process of documentary credit. The code that contains letters of credit law is the Uniform Commercial Code, which consists of eleven articles covering different aspects of commercial law. Article 5 of UCC covers the definitions and the process of a letter of credit. The first version of Article 5 in the 1950s was not considered a "code" compared to other articles in UCC, it was drafted to create a theoretical framework that is independent and could flourish later in the future. In 1995, Article 5 was revised due to "weaknesses, gaps, and errors in the original statute which compromise its relevance" (Task Force, 1990). The technologies used in documentary credit are also a reason to revise Article 5. The revised version is presented in October 1995.

The Previous Version of Article 5 of UCC

After the Sztejn case, the fraud rules are embodied in Previous Article 5, Section 5-114(2) of UCC as follows:

> "Unless otherwise agreed when documents appear on their face to comply with the terms of a credit but a required document does not in fact conform to the warranties made on negotiation or transfer of a document of title (Section 7- 507) or of a certificated security (Section 8-108) or is forged or fraudulent or there is fraud in the transaction:
> (a) the issuer must honor the draft or demand for payment if honor is demanded by a negotiating bank or other holders of the draft or demand which has taken the draft or demand under the credit and under circumstances which would make it a holder in due course (Section 3-302) and in an appropriate case would make it a person to whom a document of title has been duly negotiated (Section 7-502) or a bona fide purchaser of a certificated security (Section 8-302); and
> (b) in all other cases as against its customer, an issuer acting in good faith may honor the draft or demand for payment despite notification from the customer of fraud, forgery

> or other defect not apparent on the face of the documents but in a court of appropriate jurisdiction may enjoin such honor."

The creation of Section 5-114(2) of UCC was significant in the law of the letter of credit because it was the first time that victims can use fraud rules to protect themselves from fraudulent activities in letters of credit. The suffering of referring to other codes or principles such as the contract law or claiming the documents were not fit with the requirements of letters of credit were no longer continuing. With Section 5-114(2) of UCC, to claim the fraud rules, a party must please two conditions which are "fraud test" and "presenter test":

First, is the fraud test. The issuing bank could be stopped from paying for the documents by the court's injunction if the tendered documents appear to comply with the requirements but in fact that "document … is forged… or there is fraud in the transaction".

Second, is the presenter test. If the frauds stand out to the bank issuer, the bank could invoke the fraud rules and turns the payment request down or dishonour the documents. However, the bank could only do so if the presenter is either the beneficiary himself or another third party but not a holder in due course ((Uniform of Commercial Code, 1952), Section 3-302), or one who has taken a document of title by due negotiation ((Uniform of Commercial Code, 1952), Section 7-502) or a bona fide purchaser of security ((Uniform of Commercial Code, 1952), Section 8-302).

The issuer can only dishonour the submission once both tests are met, otherwise, in case the presenter is one of the listed immune parties, the issuer must honour the tendered documents despite the fraud (Uniform of Commercial Code, 1952). The UCC does not clarify the exact situations in which the injunction will be granted, obviously, the examination of the case law is essential (Uzzelle, 1985, p. 62). The case *Harris Corp. v. National Iranian Radio & Television* has stated the four conditions for granting the injunction are: "(1) a substantial like hood that the plaintiff will prevail on the merits; (2) a substantial treat that the plaintiff will suffer irreparable injury if the injunction is not granted; (3) threatened injury to the plaintiff must outweigh the threatened harm that the injunction may cause to the defendant; and (4) granting the preliminary injunction must not disserve the public interest" (Harris Corp. v. National Iranian Radio & Television, 1982)

The essential condition considered for the plaintiff to get the injunction would be the irreparable injury (Uzzelle, 1985, p. 63). In *Dynamics Corp. v. Citizens & Southern National Bank*, an injunction was granted, and it was considered appropriate. The Court considered that if they denied granting the injunction, the money would be moved to India as the plaintiff's remedy and the plaintiff who already appealed for bankruptcy would suffer severe disadvantages (Dynamics Corp. v. Citizens & Southern National Bank, 1973). The beneficiary was noted by the Court that he had an office in the US and "waited nearly a year before exercising its rights under the standby letter of credit" and by that, the beneficiary would not suffer severer harm if the injunction was granted (Dynamics Corp. v. Citizens & Southern National Bank, 1973)

As it might be seen, fraud rules in Article 5, Section 5-114(2) of the UCC is a remarkable milestone and is a first step for the law of letters of credit (Buckley & Gao, 2002, p. 684), however, it is not entirely faultless and remains several problems. Even when the fraud exception is drafted in the Code, one of the problems raised from the regulations is the standards of fraud and how to deal with it (Symons, 1979-1980, pp. 345-352). A frequent question among legislators is the "fraud in transaction" (Uniform of Commercial Code, 1952). This phrase raises concerns such as "what is fraud?" and "what is the transaction?" (Davidson, 2003). Consequently, the search for the standards of fraud has led to circumstances where courts have applied several definitions of fraud in letters of credit (Gao & Buckley, 2003, pp. 298-309). Some fraud standards are applied by courts as follows: "established fraud", "intentional fraud" or "egregious fraud" (Gao & Buckley, 2003, pp. 298-309) etc.

Egregious fraud:

The case *New York Life Insurance Co. v. Hartford National Bank & Trust Co.* mentioned the "egregious fraud" first. The real estate developer had to pay liquidated damages in case the developer could not fulfil his obligation to pay the plaintiff on time by a standby letter of credit for the interest of the applicant. To get payment, the applicant must present a document signed by the applicant stating that the liquidated damages were due. The documents complied with the requirements and were presented by the plaintiff. They were turned down by the bank even though the developer did not pay on schedule. The plaintiff accused the defendant of unlawful dishonour but did not mention the fraud within their allegations (New York Life Ins. v. Hartford Nat. Bank Trust, 1977).

The word "egregious fraud" appeared in the judgment of the Supreme Court of Connecticut stating that there was no fraud in this case. Under this judgment, "egregious fraud" means "must be narrowly limited to situations [of fraud] in which the wrongdoing of the beneficiary has so vitiated the entire transaction that the legitimate purposes of the independence of the issuer's obligation would no longer be served" (New York Life Ins. v. Hartford Nat. Bank Trust, 1977). As can be read within the interpretation, egregious fraud is only applied in specific circumstances where the beneficiary has violated the whole transaction in which the independent obligation of the bank has no longer served its natural intention (New York Life Ins. v. Hartford Nat. Bank Trust, 1977). As can be seen, fraud rules could refer once egregious fraud is found in cases. However, egregious fraud was mentioned in the case where no fraud is involved in documents or the underlying contract. In *New York Life Insurance Co. v. Hartford National Bank & Trust Co.,* because fraud did not happen, the court mentioned egregious fraud was "mere dicta" (Gao & Buckley, 2003, p. 301). It is noticeable that even the court acknowledges fraud rules and fraud standards, however, they hesitate to apply them in the conflicts of letters of credit where fraud is involved (Gao & Buckley, 2003, p. 301).

Intentional fraud

The concept of "intentional fraud" is mentioned in the case *NMC Enterprises v. Columbia Broadcasting System, Inc.* There was a commercial letter of credit issued in favour of the defendant to provide finance to buy the stereo receivers. However, when the plaintiff received the goods, he took legal action instantly to ask for injunctive relief from the court to stop the payment progress of the letter of credit before the defendant, which was the beneficiary, tendered the documents.

According to the plaintiff's allegations, the performance of stereo receivers was lower than the expectation he was assumed to get from the brochures. To prove his claims, a testing laboratory was hired to test and confirm his accusations (NMC Enterprises v. Columbia Broadcasting System, Inc, 1942). The Supreme Court of New York granted the requested injunction even though recognizing the accusation regarding the quality of the receivers was not enough to establish an injunction. They said:

> "Where no innocent third parties are involved and where the documents or the underlying transaction are tainted with intentional fraud, the draft need not be honored by the bank, even though the documents conform on their face and the court may grant injunctive relief restraining such honor. " (NMC Enterprises v. Columbia Broadcasting System, Inc, 1942)

Intentional fraud requires (1) a presentation that is different from the fact, (2) the awareness of unscrupulous parties about the fraud and (3) efforts to convince other parties to act upon the misinterpretation (Gao & Buckley, 2003, p. 303). Hence, to prove that intentional fraud is involved in the process, the plaintiff must demonstrate fraudulent activities. Compared to egregious fraud, it seems that the standards of intentional fraud were not as high as the standards of egregious fraud. In *NMC Enterprises v. Columbia Broadcasting System, Inc.,* the fraud rules were applied when the buyer had clearly stated that even though the seller knew the quality of the stereo receivers was different but he still promoted and convinced the buyer to enter the contract (Gao & Buckley, 2003, p. 304).

Established fraud

The established fraud is mentioned in the Edward Owen case, Browne LJ stated that Lord Denning had accepted his commentary in *Bank Russo-Iran v. Gordan Woodroffe & Co* (cite case). Browne LJ has clarified that fraud rules could be invoked by the issuing bank once the documents presented by the beneficiary are forged, the banks are enabled to turn the documents down once they find out about fraud before paying (Davidson, 2003, p. 36). They also are entitled to reclaim their money back if they discovered the fraud after payment. According to Browne LJ, claiming there was a fraud was not enough, the fraud must be "established" and "very clearly established" (Edward Owen Engineering Ltd v Barclays Bank International Ltd, 1978).

The broader approach

This definition was mentioned in D*ynamics Corp. of America v. Citizens & Southern National Bank*. In this case, the plaintiff sold defence-related types of equipment to the Indian government through a sale contract. The Citizens & Southern National Bank, the defendant, was required to issue a standby credit which promised that the bank shall honour the documents drawn by the Indian government. The documents must include a certification from the Indian Government stating that the plaintiff had failed to perform its duties in the sale contract. Unfortunately, in 1971, India and Pakistan had a conflict that led to a war and the US government banned the delivery of military supplies to these two regions. Hence, the plaintiff could not ship the equipment to Indian Government (Dynamics Corp. v. Citizens & Southern National Bank, 1973). The Indian Government then submitted a certificate along with the documents which comply with the conditions in the credit. The plaintiff then brought the case to the court claiming that they had performed their contracted obligations. The injunctive relief was granted by the United States District Court of Georgia as follows:

> "[t]he law of "fraud" is not static and the court has, over the years, adapted it to the changing nature of commercial transaction in our society. … In a suit for equitable relief- such as this one- it is not necessary that the plaintiffs establish the elements of actionable fraud required in a suit for monetary damages… Fraud has *a broader meaning* in equity and an intention to defraud or to misrepresent is not a necessary element. Fraud, indeed, in the sense of a court of equity properly includes all acts, omissions and concealments which involve a breach of legal or equitable duty, trust, or confidence, justly reposed, and are injurious to another, or by which an undue and unconscious advantage is taken of another." (Dynamics Corp. v. Citizens & Southern National Bank, 1973)

Remarks on the standards of fraud

In general, the first version of Article 5, Section 5-114 of UCC is a well-drafted article. Both technical and merely legal concepts as well as banking practice are combined under these rules (Kozolchyk, 1979). As this version of Article 5 of UCC kept silent over the fraud standards, as result, the courts accepted several fraud standards because their views were different (Gao & Buckley, 2003, p. 309). To establish whole new regulations for letters of credit, which is a sophisticated area, legislators and lawmakers are required to perform fully their expertise and prepare detailed rules to make sure the operation of the system will continuously work. One of the most serious issues in defining fraud rules is to protect the commercial utility of the letter of credit by remaining the independent principle. Standards of fraud are very important because it is quite complicated. If we set the standards too high, fraud rules would lose their effectiveness. If the standards are too low, the applicant may use fraud rules to violate the independent principle and prevents the beneficiary from receiving his payment. Fraud standards must serve their functions for fraud rules as well as are workable for the courts.

Moreover, letters of credit users and the courts as well as the legislators are also confused about the location of fraud under the guidance of Previous Article 5, Section 5-114 of the UCC: whether the fraud should only be examined in the documents of the letter of credit, or should

it be extended to the fraud in the underlying transaction (Buckley & Gao, 2002, p. 684). Without solving these troubles, the commercial utility of letters of credit in the US might be reduced in the international trade (Flint, 2019, p. 384).

The Iranian Revolution

During the Iranian Revolution, fraud in standby letters of credit had gone through a significant change which impose a big impact on the fraud rules. Even though this thesis's scope mainly focuses on commercial letters of credit, this change is quite noticeable, and it deserves a brief analysis.

Within several standby letters of credit worth billions of dollars which the US banks had issued for years in foreign countries, the construction projects made up almost 50 per cent of them (Peter Lloyd-Davies, 1982)[82]. Standby credits are considered a simple guarantee to make sure that the beneficiaries would receive payment once the contractors fail to perform their duties which are stipulated in the contracts.

The Imperial Government of Iran in the 1970s had several large projects to rejuvenate the country. The US contractors did not miss this chance because there were billions of dollars provided for this project (Driscoll, 1979, p. 459). The Middle East Government wanted to ensure that the contractors fully performed their obligations, so they requested "suicide" standby letters of credit in favour of the Government (Herbert A. Getz, 1980, p. 196). Such standby letters of credit involved four parties which were the US contractor, the agency of the Iranian Government, a US bank, and an Iranian Bank. There shall be a contract between the US company and the Iranian Government about providing pieces of equipment or services and the Iranian agency would require a term in the contract asking the US company to provide a warranty for his performance, the value of the guarantee would fluctuate from five to ten per cent of the value of the contract (Herbert A. Getz, 1980, p. 196). Then the US company required a US bank to issue a standby letter of credit in favour of the Iranian Government in case the US company did not perform its obligations well. An Iranian bank would be asked to participate in the standby letter of credit and become a counter-guarantee to make sure that the Iranian Government would be honoured by the bank once the dispute happened. Once the dispute happened, the Iranian bank would pay for the Iranian Government under the standby, then the Iranian bank could have sought reimbursement from the US bank and the US company must reimburse the US banks (Gao, 2002, p. 79).

Iran Revolution happened in 1979 and the new Islamic Republic of Iran blocked several regulations issued by the former government. Unfortunately, this situation also prevented the performance of the contracts signed before. The US companies, in the fear of being charged in their accounts by the claiming payments of the new Islam Government for not performing their contracts in Iran, took legal actions to enjoin the payments under standby letters of credit by

[82] The American banks had poured over 11 billion US Dollars to overseas transactions and half of it is for construction agreements.

invoking the fraud rules. The legal history had divided into two phrases which were "the pre-hostage cases" and "the post-hostage cases". In the pre-hostage cases, the US companies tried to use the "only marginal success in the court" (Zimmet, 1984, p. 927). In this stage, there were only two cases that were granted with the injunctions and these two cases were vacated (Gao, 2002, p. 79)[83]. Most of the cases were denied or only received "notice injunction" which meant that the courts prohibited the banks from paying the Iranian beneficiaries unless they had noticed the American companies. The popular reason of the courts for the rejection of granting the injunctive relief was because the US companies had failed in pointing out fraudulent activities or hideous acts of the beneficiary.

However, compared to the pre-hostage, the circumstances in the post-hostage were changed due to the hostages at the US Embassy in 1979, and the view of the courts changed dramatically in granting injunctive relief. Among 14 cases that had asked for injunctions, 12 of the cases received the injunctions, and the rest was denied (Zimmet, 1984, pp. 78-82). Furthermore, in the aforesaid twelve cases, there were only three cases with written opinions, two were decided without formal written judgments and the rest of the cases were issued without the opinions. The courts began to grant injunctive reliefs based on "the Iranian demand for payment threatened the contractors with immediate irreparable injury" (Zimmet, 1984, p. 927).

After the Iran-the United States Claims Tribunal in 1981, there were a lot of allegations sent to the courts, but the injunction litigations were not stopped by the US courts and the courts continued to grant the injunctive relief. For those cases with injunctions, the letter of credit experts partly agreed with these decisions. In *Touche Ross & Co. v. Manufacturers Hanover Trust Co.,* the Ministry of War of the Imperial Government had a contract with the plaintiff to audit the financial aspects of several contractors working with the Government. Within this contract, there was a term referred to as force majeure, and this term also allowed all guarantees to be terminated (Touche Ross & Co. v. Manufacturers Hanover Trust Co, 1980). Once the revolution happened, the Iranian required the bank to honour the standby and the Iranian Bank sought reimbursement from the US bank. Touche brought the allegation to the court asking for injunctive relief and the court granted as follows:

> "[A]s a result [of the cancellation of the contract], the guaranty has been released, and no legitimate call could be made on the guaranty or the letter of credit…
> As all financial institutions in Iran, including Bank Saderat, have been nationalized, Bank Saderat is owned by the Islamic Republic of Iran. Bank Saderat could not have legitimately paid on the guaranty, as Bank Saderat would be simply paying itself. Therefore, any call on the letter of credit would be fraudulent." (Touche Ross & Co. v. Manufacturers Hanover Trust Co, 1980)

The court granted its injunction based on two elements:

[83] These two cases are John Carl Warnecke & Assocs v. Bank of America Nat'l Trust & Savings Ass'n, [No. 749626 ND Cal 17 April 1979]; and KNW International v. Chase Manhattan Bank NA [No. 79 Civ 1067 SDNY 29 March 1979].

- The dispute of the honouring of the standby was no longer legitimate since the contract was cancelled; and,
- After the revolution, the Iranian Bank belonged to the new government, and it could not be considered itself as before. Hence, the requirement for honouring the standby could be considered fraudulent.

With this point of view, the court made a new alert for all letters of credit commentators around the world (Zimmet, 1984, p. 927). This view was considered too flexible and not stable, which reduced the commercial utility of letters of credit, furthermore, it "take[s] the fraud rules very long way from its purpose" (Gao, 2002, p. 82).

The Revised Version of Article 5 of UCC

Even though Article 5 of the Uniform Commercial Code is adopted in most states in the US, some issues remain from Previous Article 5 of UCC. Such problems are seen through different lenses by the bankers in the US who use the UCC regulations and are supplied by the contract law in the common law. Their foreign partners, in contrast, normally use UCP in letters of credit (Barnes & Byrne, 1995). Previous Article 5 also gave few instructions relating to which fraud standards should the courts use to identify the problems[84]. Because the technology in letters of credit was developing as well as the need for uniformity of fraud standards, the practice of letters of credit needed consistency between domestic law and international law. In 1986, the UCC Committee of the American Bar Association (ABA") and the United States Council for International Business ("USCIB") formed a group of lawyers called Task Force to review the case law, trade customs, and practices as well as investigated the new technologies in the letter of credit from Previous Article 5. The Task Force had stated that the trial courts in the US had issued several injunctive reliefs which stopped the payment obligations of the issuer. The Task Force had recommended having a uniform provision defining the foundation for issuing the injunction (Task Force, 1990).

With those efforts, the rule of fraud is demonstrated in Article 5, Section 5-109 as follows:

> "(a) If a presentation is made that appears on its face strictly to comply with the terms and conditions of the letter of credit, but a required document is forged or **materially fraudulent**, or honor of the presentation would facilitate a material fraud by the beneficiary on the issuer or applicant:
> (1) the issuer shall honor the presentation, if honor is demanded by (i) a nominated person who has given value in good faith and without notice of forgery or material fraud, (ii) a confirmer who has honored its confirmation in good faith, (iii) a holder in due course of a draft drawn under the letter of credit which was taken after acceptance by the issuer or nominated person, or (iv) an assignee of the issuer's or nominated

[84] As stated above, the Section 5-114(2) did not mention about the standards of fraud, which caused several standards and confused the courts in applying the fraud rules.

person's deferred obligation that was taken for value and without notice of forgery or material fraud after the obligation was incurred by the issuer or nominated person; and
(2) the issuer, acting in good faith, may honor or dishonor the presentation
in any other case.
(b) If an applicant claims that a required document is forged or materially fraudulent or that honor of the presentation would facilitate a material fraud by the beneficiary on the issuer or applicant, a court of competent jurisdiction may temporarily or permanently enjoin the issuer from honoring a presentation or grant similar relief against the issuer or other persons only if the court finds that:
(1) the relief is not prohibited under the law applicable to an accepted draft or deferred obligation incurred by the issuer;
(2) a beneficiary, issuer, or nominated person who may be adversely affected is adequately protected against loss that it may suffer because the relief is granted;
(3) all of the conditions to entitle a person to the relief under the law of this State have been met; and
(4) on the basis of the information submitted to the court, the applicant is more likely than not to succeed under its claim of forgery or material fraud and the person demanding honor does not qualify for protection under subsection (a)(1).”

As has been seen, Revised Article 5, Section 5-109 of UCC has adjusted some problems with fraud.

First, the process of letters of credit is only suspended once fraud is discovered in two circumstances: the issuer decides to turn the presentation of documents down, or the applicant asks the courts to grant the injunction to block the payment.

This regulation is similar to Previous Article 5 since it is not an obligation but a possibility for the issuer to turn the payment requirement down when fraud is invoked. To have a better result in postponing the payment process, the applicant might ask for the court's injunctions.

Second, fraud standards, one of the most argumentative issues, which is the unsolved problem in the previous version of Section 5-114(2) were tackled. Section 5-109 presented the “material fraud”. This definition is tightened, which is better than disposing of the likelihood of the injunction for fraud. “Section 5-109 makes it marginally more difficult for an applicant to get an injunction than would have been true under the old law. To get an injunction, the applicant must show not merely fraud but 'material fraud.” (White, 1995, p. 108).

However, the definition of “material fraud” is not clear and as Mark S. Blodgett and Donald O. Mayer said, they “do not expect that the use of ‘material fraud’ (rather than ‘fraud in the transaction,’ ‘egregious fraud,’ or ‘intentional fraud’) will clear up the confusion” (Blodgett & Mayer, 1998, p. 459). However, the Official Comment had listed some rules from some cases of law to define what actions could be considered material fraud (Itek Corp. v. First Nat. Bank of Boston, 1983) (Intraworld Industries v. Girard Trust Bank, 1975) (Roman Ceramics Corp.

v. Peoples Nat. Bank, 1983) (Itek Corp. v. First Nat. Bank of Boston, 1983)[85] which include the honour has no actual foundation (Dynamics Corp. v. Citizens & Southern National Bank, 1973)[86], the whole transaction is damaged by fraudulent activities of the beneficiary (Intraworld Industries v. Girard Trust Bank, 1975)[87] and the underlying contract clearly expresses that the beneficiary is not allowed to draw on in that specific situation (Itek Corp. v. First Nat. Bank of Boston, 1983)[88].

Considering the Official Comment to the UCC, the "material" also could be understood as "significant to the participants to the underlying transaction" (Baird, et al., 2002, p. 545). Based on the definition and the guidance of the Official Comment, the courts must search the underlying contract to determine the pieces of evidence submitted and examine the existence of the fraud, furthermore, the court must determine if the fraud is material. The burden of proving the evidence relating to fraud depended on the applicant.

However, the examination of the underlying contract contrasts with the original intention of the independent principle, which separates the sales contract and the letter of credit (Dolan, 1999, p. 532). The fraud standards which invoke the injunction of the court must be high enough to protect the independent principle and the judges must be aware that the injunctive relief is extraordinary and only be issued in specified circumstances (Baird, et al., 2002, p. 547).

Third, the UCC saves the innocent parties, known as holders in due course who have acquired the documents without knowing the fraud.

The buyer shall bear the burden of risks, however, there are third parties in the letter of the credit process. They may be the transferees or the assignees; they also could be the applicant's creditors. Once fraud is involved, these parties might be affected as well. Hence, to retain the rights of such parties, the UCC has created high standards to invoke the fraud rules as well as establish an exemption to protect innocent third parties.

Section 5-109(a) (1) includes four types of participants who are immune from the fraud rules:

> "(i) a nominated person who has given value in good faith and without notice of forgery or material fraud,
> (ii) a confirmer who has honored its confirmation in good faith,

[85] In the case *Itek Corp. v. First Nat'l Bank of Boston*, the holding stated that the injunctive relief would be deceived by the court to prevent the issuer to honor the documents while the beneficiary "did not even have a colorable claim".
[86] In the case *Dynamics Corp. of Am. v. Citizens & S. Nat'l Bank*, the court noted that the beneficiary could not take advantages on the situations and took the plaintiff's money without basic in fact.
[87] In the case *Intraworld*, the court noted that the injunctive relief could only be issued in case the entire transaction was vitiated which made the original obligation of the issuer- which was the independent principle- become disappear.
[88] In the case *Itek Corp. v. First Nat'l Bank of Boston*, the fraud exception "recognizes the unfairness of allowing a beneficiary to call a letter of credit under circumstances where the underlying contract plainly shows that he is not to do so."

(iii) a holder in due course of a draft drawn under the letter of credit which was taken after acceptance by the issuer or nominated person, or
(iv) an assignee of the issuer's or nominated person's deferred obligation that was taken for value and without notice of forgery or material fraud after the obligation was incurred by the issuer or nominated person."

- *Nominated person*

Under Section 5-102(11) of UCC, the nominated person is the one who is chosen by the issuer to advise, accept, honour, and negotiate under the letter of credit (Uniform of Commercial Code, 1952). By nominating a person in the letter of credit, the issuing bank gives that person the credit to give value or to pay for the beneficiary. The nominated person must receive the stipulated documents from the beneficiary before the letter of credit is expire unless the credit states different requirements (Baird, et al., 2002, p. 531).

The nominated person is not the presentative of the issuing bank but rather a separate individual who engages in letters of credit as "in rare cases … an agent of the issuer and its act might be the act of the issuer itself" (Baird, et al., 2002, p. 531). Once the nominated person decides to honour the documents and sets up a settlement in good faith then he has the right to seek reimbursement from the issuing bank, whether fraud is involved or not.

- *The confirmer of the letter of credit*

The beneficiary normally wants to receive money in their currency and be guaranteed by a local bank. So, the issuer will authorize a local bank as a confirming bank (or known as a confirmer) to honour the submission of the documents. The duties of confirming the bank include checking the documents, accepting them, and paying for the beneficiary or negotiating. Confirmer is in the same position as the issuer from the perspective of the beneficiary and third-party presenters so that its rights and obligations are the same as the issuing bank.

In the Revised Article 5 of UCC, the confirming bank is protected from fraud rules. Within Section 5-109(a)(1)(ii), if the confirmer acts with good faith and submits the complied documents, then even though the fraud is invoked, the issuer must reimburse the confirmer.

The case *Banco Santander SA v. Bayfern Ltd*. might be a good example of the legal status of the confirmer. This case was decided from the England authority's view; however, it is worth considering and it points out the differences between the approach of America and England in fraud rules. Napa Petroleum, the buyer, purchased crude oil from Bayfern Limited, the defendant, and a letter of credit was chosen to provide the financing for parties (Banco Santander v. Bayfern Ltd., 1998). The buyer applied for a letter of credit in Banque Paribas in favour of the seller. The expiration day of the letter of credit was the 15th of September 1999 and the beneficiary would receive the payment 180 days after the issuing date of the letter of credit. Banco Santander, the plaintiff, was asked to be the confirmer of the credit, and Banque Paribas would provide the instructions. The confirmation, which was sent to Bayfern, also

suggested a discount for the credit. The defendant then submitted the documents to the defendant's bank and asked for a discount and the defendant's bank agreed. Banque Paribas was not informed in both events of the discount (Banco Santander v. Bayfern Ltd., 1998).

The plaintiff then sought reimbursement by sending the documents and was refused to get paid because of forged documents. Banco Santander then applied for a judgment against Banque Paribas claiming that the issuer was bound to reimburse in light of Article 14(a) of UCP 500 even though the fraud was found before the expiration day of credit. The court then concluded that the credit did not require Banco Santander to discount the credit, so the discount was not a breach of mandate. The Appellate Court concluded that Banque Paribas was authorized to refuse the reimbursement because the right to reimbursement was raised only at the expiration date (Banco Santander v. Bayfern Ltd., 1998).

The Appellate Court then declared as follows:

> "Santander had no authority to negotiate from Paribas to discount and did not seek it. It was something they were entitled to do on their own account. If they had not chosen to discount and had waited until 27 November, they would have had a defence. ... If a confirming bank in the position of Santander wishes to be free to give value for documents when it accepts the documents, it can do so either by insisting on the use of an acceptance credit or by insisting on obtaining authority to negotiate and confirmation of reimbursement if it does." (Banco Santander v. Bayfern Ltd., 1998)

The Court also referred to the *European Asian v. Punjab & Sid Bank* case:

> "... if Santander had informed Paribas that it had discounted and had received confirmation from Paribas that Paribas would still reimburse on 27 November 1998, Paribas would not be able to raise the fraud exception because they would be estopped from disputing Santander's authority to discount." (Banco Santander v. Bayfern Ltd., 1998)

The opinion of the Court stated that once a draft was called for and the confirmer became a holder in due course with his good faith then he was authorized to rely on the documents and sought reimbursement from the issuer even if fraud was found before the maturity date. However, no documents were provided to prove that Santander was a holder in due course.

Lord Justice Waller declared as follows:

> "I have ultimately concluded that if the parties agree for whatever reason that they will not provide a negotiable instrument, and do not provide by terms of the trade or even by the express terms of the instrument itself the protection for assignees that a negotiable instrument would provide, they must live with the consequences." (Banco Santander v. Bayfern Ltd., 1998)

Apart from the opinion of the English authority that this case was well-founded, the banking community had raised several criticisms (Bob Foster, 1999) (Johnson & Aharoni, 2000) (Barnes, 2000). The parties in letters of credit were expected to continue their behaviours based on their authority in the credit to meet the expectations of the others.

The American Authority had a different view in deciding the Banco Santander case as "US letter of credit bankers and lawyers answered the question posed in Santander and similar questions, in which the desire to deter fraud must be balanced against the desire that non-fraudulent demands under the letter of credit be honoured, with certainty" (Barnes, 2000). If Banco could prove that its payment was supported with good faith, then Banque Paribas should have been reimbursed under the UCC.

- *Holders in due course*

Under the definition in Section 3-302 of UCC, the holders in due course are those who:

- give the draft value before the injunction notice,
- have a good faith, and
- does not know about the fraud at a certain time.

It is normally recognized that the holders in due course should be protected from the injunctive relief of the courts. In the Sztejn case, the protection is mentioned that the holder in due course should be protected "even though the primary transaction was tainted with fraud" (Sztejn v. Henry Schroder Banking Corp. , 1941).

The holders in due course along with the good faith might be well emphasized in *Brenntag International Chemicals, Inc. v. Bank of India*. In this case, the negotiating bank honoured the documents in the bad faith because they were aware of fraud. The payment between Brenntag International Chemicals, the plaintiff, and Petro Pharma was assured by a pay-at-sight standby letter of credit issued by Norddeutsche Landesbank. Bank of India, the defendant, was the negotiating bank (Brenntag International Chem. v. Bank of India, 1999).

After that, the beneficiary required a discount from the negotiating bank and presented documents, and there were some discrepant documents. The negotiating bank still honoured the documents even though there were so many defaults. Petro was given a loan by the Bank of India under an independent contract. Later, Petro could not ship the goods to Brenntag because of financial difficulties which led to the cancellation of the contract with Brenntag. Afterwards, Petro submitted a default letter signed by a person who had resigned since the Bank of India required so. Petro informed the Bank of India that there were no shipments of goods so Brenntag could not be in default. Despite the notice from Petro, the documents were still submitted by the Bank of India. The issuer then turned the requirements down and Brenntag brought the case to the court asking for injunctive relief to stop the payment of the issuer.

The court stated that:

> "The evidence also indicates that Bank of India knew that these documents were noncompliant and materially inaccurate at the time it obtained them, knew that they remained false and fraudulent at the time it sought to collect upon them. ... For these reasons, there was ample reason for the district court to conclude that *Bank of India was not entitled to payment from Norddeutsche Landesbank and was not a holder in due course.*" (Brenntag International Chem. v. Bank of India, 1999)

- *The assignee of the deferred payment obligation*

Section 5-109(1)(a) of UCC mentioned "assignee of the issuer's or nominated person's deferred obligation that was taken for value and without notice of forgery or material fraud after the obligation was incurred by the issuer or nominated person" is protected from the fraud rules (Uniform of Commercial Code, 1952).

The kind of letter of credit which will be paid on a planned day since the complied documents are submitted to the bank is called deferred payment. However, the beneficiaries normally want to receive money once they submit the documents so that they can ask the issuing bank to determine a bank "to advance to it all or part of the funds owed under the deferred payment obligation or to discount the deferred payment obligation by assigning the proceeds of the letter of credit" (Gao, 2002, p. 151), the such bank is called an assignee.

However, there are differences between the English Authority and the American Authority. The court declared in *Banco Santander* that confirming bank would become an assignee once they discounted the documents, which meant that the confirming bank stood in the same position as the beneficiary in the issuing bank's orientation. Hence, once the fraud was committed by the beneficiary, the confirming bank had the right to seek reimbursement. This view of the English court is completely contrary to the American point of view.

The legislator in letters of credit field had expected that the deferred payment could be defined in the UCP 600, however, the details of the definitions and the positions of the confirmer and the nominated person of this kind of credit are still not mentioned clearly under the UCP 600.

Fourth, if documents are claimed forgery or fraudulent by the applicant and he wants to enjoin the honour, issuing bank could be enjoined from honouring submitted documents by temporary or permanent injunctions of the courts under four conditions in Section 5-109(b).

With all the improvements, the Revised Article 5, Section 5-109 of UCC becomes one of the extensive regulations about rules of fraud in the letter of credit law and is used widely. Article 5 was considered a good legal source for modern letters of credit law (Buckley & Gao, 2002, pp. 683-684).

7.5. The Law of Letters of Credit in the People's Republic of China

7.5.1. The History

According to the independent principle- the milestone of letters of credit, the documents submitted by the beneficiary must conform to the requirements from the letter of credit so that the beneficiary could obtain the payment, however, there is an exception – the rules of fraud can withhold the reimbursement once the fraud is found.

It had been years since the practice of letters of credit in the People's Republic of China (hereinafter referred to as "P.R.C.") was criticized by international banks and the letter of credit experts because they claimed that the Chinese applicants and the banks tried to use fraud rules to avoid their payment obligation (International Chamber of Commerce, 1996). The necessity to have fraud rules and their application in the Chinese legal framework was obvious, partly because the practice of the courts was found persistent (Gao, 2007, p. 1068). And it was not until late 2005 that P.R.C. had its first proper rules for letters of credit (Gao, 2007, p. 1068).

The problems with fraud rules in P.R.C.'s letters of credit cases began with *Yuegang Agricultural Resources Development Co. v. Japanese Technology & Science Co.,* in 1986. In the underlying contract, the payment between parties was secured by a letter of credit worth ¥216 million. The plaintiff (Yuegang) claimed the feedstuffs of the machines delivered by the defendant Japanese Technology & Science Co., did not meet the requirements stipulated in the sales contract. The plaintiff then brought the case to the court and requested injunctive relief to stop the reimbursement under the letter of credit.[89] An injunctive relief was then issued by the court (Yuegang Agricultural Resources Development Co. v. Japanese Technology & Science Co., 1986).

The letter of credit specialists was extremely disappointed with this decision. Fraud was not cited in the case. The main allegation of the plaintiff was about the condition of goods, which was a breach of warranty so fraud rules should not be mentioned. Unfortunately, the Yuegang case was the orientation of the Courts in the P.R.C. in the early period (Gao, 2007, p. 1071).

In the early years, when commercial or civil cases were brought to the courts in P.R.C., the plaintiff usually sought a property conservancy order to freeze the belongings of the defendant under the light of the Civil Procedure Law of the P.R.C. (hereinafter referred to as "CPL of PRC")[90] (China People's Congress, 1991). Under Article 93 of THE CPL of P.R.C.[91], once the

[89] The English translation of the case *Yuegang Agricultural Resources Development Co. v. Japanese Technology & Science Co.,* is taken from the translation of Xiang Gao (2007)

[90] The English translation of CPL of PRC is borrowed from the translation of Civil Procedure Law of the People's Republic of China from the China Internet Information Center. See more at: http://www.china.org.cn/english/government/207339.htm.

[91] Article 93 of The CPL of PRC provides:
An interested party whose lawful rights of interests would, due to urgent circumstances, suffer irretrievable damage without immediately applying for property preservation, may, before filing a lawsuit applying to the people's court for the adoption of property preservation measures. The applicant must provide security; if he fails to do so, his application shall be rejected.

Court accepts the application, in 48 hours, the judges must issue a decision, or in compelling situations, the order shall be enforced (China People's Congress, 1991)[92].

The courts were frequently asked to enjoin the payments of the issuing banks or confirming banks under letters of credit. The issuers and confirmers were usually considered third parties in letters of credit and their accounts which were used for the letter of credit payment would be frozen for the sake of property preservations. In the early years of the economic transformation in P.R.C., the courts would naturally observe the instructions from the CPL of PRC, under Article 92[93] and Article 94[94] of THE CPL of PRC (China People's Congress, 1991), they would suspend the process of paying off the bank accounts of letters of credit without considering the independent principle of letters of credit. The independent principle as well as the special mechanism of letters of credit were wholly neglected since the judges knew little about the economic utilities of this instrument. As a result, when the economy of China started to bloom in the 1970s (Gao, 2007, p. 1071), the courts in P.R.C. received several criticisms from the Chinese banks since they kept underestimating the independent principle and suspended the payments of letters of credit. The reason for this wave of objection was partly because the Chinese banks realized that their international reputation was threatened and the economic benefits of letters of credit were jeopardized since the court periodically meddled with the letter of credit payment (Gao, 2007, p. 1072).

The 1989 Summary

Gradually, based on the conscious of the structure of letters of credit of the courts, the Supreme People's Court of P.R.C. (hereinafter referred to as "SPC of PRC") constantly recognized that the situation where courts interrupt the payment of letters of credit and took letters of credit very much alike normal commercial instruments were not legitimate (Gao, 2007, p. 1073).

Therefore, in December 1988, at the National Forum on the Adjudication of Economic Cases Relating to Foreigners and People from Hong Kong and Macao in the Coastal Region, the issue of pausing the payment was discussed. Later, on June 12, 1989, *the Summary of the National*

After receiving an application, the people's court must make an order within 48 hours; if the court orders the adoption of the property preservation measures, the execution thereof shall begin immediately.

[92] Under this thesis, to present the situations in China regarding property preservation in the early years before the fraud rules of China is issued, the author shall focus on the of Civil Procedure Law of the People's Republic of China issued in 1991. The Civil Procedure Law of the People's Republic of China is revised in 2017. See more at: http://cicc.court.gov.cn/html/1/219/199/200/644.html. The new versions of Articles 92, 93 and 94 of The CPL of PRC 1991 are revised and relocated in Articles 100, 101 and 102 of CPL of PRC 2017.

[93] Article 92 of The CPL of PRC provides:

In the cases where the execution of a judgment may become impossible difficult because of the acts either party or for other reasons, the people's court may, at the applications of the other parties, order the adoption of measures for property preservation. In the absence of such applications, the people's court may at itself, when necessary, order the adoption of measures for property preservation.

In adopting property preservation measures, the people's court may enjoin the applicant to provide security; if the applicant fails to do so, his application shall be rejected

[94] Article 94 of The CPL of PRC provides:

Property preservation shall be limited to the scope of the claims or to the property relevant to the case. Property reservation shall be affected by sealing up, distraining, freezing or other methods as prescribed by the law.

Forum on the Adjudication of Economic Cases Relating to Foreigners and People from Hong Kong and Macau in the Coastal Region was issued by the SPC of P.R.C (hereinafter referred to as "1989 Summary"). In the 1989 Summary, the foundation of the letter of credit law in P.R.C was provided, and the fraud rules were first mentioned in the summary in paragraph 3(4)(ii) as follows:

> "In view of the practice at home and abroad, if sufficient evidence shows that the seller is using the underlying contract to defraud the buyer, and the Chinese bank has not paid within a reasonable time, a people's court may freeze the payment of the letter of credit upon the requirement of the buyer. However, a people's court should not freeze the payment of an acceptance credit when a time draft presented thereunder has already been accepted by the Chinese bank, as the obligation of the Chinese bank in such a situation has become unconditional under the law of negotiable instruments. […] A people's court should follow the same steps mentioned when it receives an application from a Chinese foreign arbitration agency for the freezing of the payment of a letter of credit."

In the 1989 Summary, two serious purposes disclosing the rules of fraud and letters of credit law in P.R.C were mentioned:

First, the Summary confirmed that the letter of credit was an exclusively financial device (Supreme People's Court of People's Republic of China, 1989). The independent principle was also brought up and its importance was emphasized in the Summary (Gao, 2007, p. 1074).

Second, essential features related to fraud rules were first mentioned:

- Once adequate pieces of evidence were shown to the court which revealed that fraud was found in the underlying contract which was done by the beneficiary and the underlying transaction was being used to defraud the applicant, then the Court could grant injunctive relief to suspend the payment (Supreme People's Court of People's Republic of China, 1989).

- Once the remittance was made, the court could not stop the payment. This provision also applied to the situation in which the documents were presented and accepted by the bank, even though there was fraud in the transactions (Supreme People's Court of People's Republic of China, 1989).

Based on these new provisions, the courts in P.R.C, especially those at high levels, when handling the cases related to letters of credit including fraud, could recognize the importance of the extraordinary characters of letters of credit and granted their judgments with caution when they were asked to enjoin payment in letters of credit. However, the 1989 Summary was underestimated because it did not have the enforcement of law and was only a policy statement of the SPC of PRC (Gao, 2007).

7.5.2. The Rules of the Supreme People's Court Concerning Several Issues in Hearing Letter of Credit Cases

A. Introduction

Under the pressure of economic reform in P.R.C., No. 4 Civil Division (hereinafter referred to as "Division") is set up to meet the requirements of handling commercial cases relating to foreign partners and maritime affairs. One of the main preferences of this Division is to build fundamental provisions which are used to guide the courts in P.R.C. to treat commercial cases with foreign parties and maritime cases properly (Gao, 2007, p. 1077). After the Division is formed, the demand for a perfect legal interpretation relating to the letter of credit field is obvious.

The Supreme People's Court in P.R.C. had tried to fill the lack of consistency in the letter of credit rules and courts' practice. The Supreme People's Court then declared *The Rules of the Supreme People's Court Concerning Several Issues in Hearing Letter of credit Cases* dated November 14, 2005, [95] (hereinafter referred to as "The 2005 Rule") (Supreme People's Court of the People's Republic of China, 2005). One of the reasons was the accusations of the Chinese banks since their positions in the international trade were in danger. According to Xiang Gao (2007), the Chinese banks had performed remarkable efforts to campaign the process for years and had put a lot of effort into commenting on the draft. The Banking Commission of ICC China held an important conference in January 2000 in Beijing for judges and commissioners of fourteen major banks in China to indicate their problems with the payment suspension of letters of credit of the courts when fraud was involved in.

The 2005 Rules is a group of judicial interpretations. The Supreme People's Court of P.R.C. has prepared specific instructions for several situations including specific cases to particular rules or peculiar guidance in special fields that the law has not reached. The whole 2005 Rules covers the entire letters of credit area, but its main target is the fraud rules. It mainly focuses on problem-solving rather than issuing a statute for a letter of credit. However, the 2005 Rules are not considered law but in realistic awareness, it is law since it has the enforcement of law and the courts keep citing it in their decisions (Gao, 2007, p. 1068).

The 2005 Rules cap most of the problems of scams in letters of credit including fraud standards, those who are exempt from exercising fraud rules, which courts could receive the applications from what parties, and other issues. In general, fraud rules under the 2005 Rules include both procedural and substantive matters of the letter of credit law (Gao, 2007, p. 1077).

B. The Regime of the 2005 Rules

[95] The English translation of *The Rules of the Supreme People's Court Concerning Several Issues in Hearing Letter of credit Cases* is borrowed from the translation of AsianLII. See more at: http://www.asianlii.org/cn/legis/cen/laws/potspcosicttocodoloc1163/

Standards of fraud

The only exception to the independent principle is fraud rules. Fraud rules are usually used to avoid scammers taking advantage of other parties from the sales transaction and letters of credit. Fraud rules will be invoked once a scam is involved in the agreements. A proper approach to fraud rules will create a stable apportionment of the parties' risks (Houten, 1984, p. 385). Detailed rules are needed to build a legal structure for a sophisticated field like the law of letters of credit, and the legislators need to fully understand this field. To consider in which situations fraud rules could be involved in the court decisions, the judges should interpret the definition of fraud carefully or seriously consider the types of fraud that can be recognized.

One of the problems which confused many courts and legislators was the fraud standards (Symons, 1979-1980, pp. 345-352). Consequently, the hunting for the standards led to the circumstance that courts had applied several definitions of fraud in the letter of credit law to retain its economic advantages (Gao & Buckley, 2003, pp. 298-309). There were some fraud standards that were applied by courts in the US such as "egregious fraud" (New York Life Ins. v. Hartford Nat. Bank Trust, 1977) or "intentional fraud" (NMC Enterprises v. Columbia Broadcasting System, Inc, 1942). While some courts considered that the standards of fraud must be strict in order not to violate the independent principle, others chose to apply more flexible standards. With the diversity of types and standards applying for fraud rules, these models represented the points of view of legal legislators protecting the independent principle of "the importance to international commerce of maintaining the principle of the autonomy of documentary credits…" (Bank of Nova Scotia v. Angelica-Whitewear Ltd., 1987).

In defining fraud in commercial and civil cases in P.R.C., the courts usually refer to Article 68[96] of the Interim Opinion of the Supreme People's Court Concerning the Implementation of the General Principles of the Civil Law of the P.R.C.[97] (herein referred to as "IOGPCL"). Considering that letters of credit are a special economic device and the case studies for years of Chinese courts, Article 8 of the 2005 Rules[98] has created a new point of view in what situations the fraud rules could be invoked as follows:

> "The letter of credit fraud shall be determined as constituted under any of the following circumstances:
> (i) The beneficiary forges documents or provides documents containing false information.

[96] Article 68 provides:
An act is deemed an act of deceit if one party willfully misrepresents to or deliberately conceals from another party facts and thereby induces the other party to make a mistaken expression of intention.
[97] The English translation of Article 68 is taken from the translation of Whitmore Gray and Henry R. Zheng for Opinion of the Supreme People's Court on Questions Concerning the Implementation of the General Principles of Civil Law of the People's Republic of China (Translation). See more at: https://repository.law.umich.edu/articles/1542/
[98] The English translation of *The Rules of the Supreme People's court Concerning Several Issues in Hearing Letter of credit Cases* is borrowed from the translation of AsianLII. See more at: http://www.asianlii.org/cn/legis/cen/laws/potspcosicttocodoloc1163/

(ii) The beneficiary maliciously refuses to deliver the goods or delivers goods of no value.
(iii) The beneficiary provides false documents by colluding with the applicant or a third party and there isn't any true basic transaction; or
(iv) Other circumstances under which letter of credit fraud is conducted." (Supreme People's Court of the People's Republic of China, 2005)

As can be seen, fraud standards under the 2005 Rules are defined a bit differently from fraud rules under the Civil and Commercial provisions. The 2005 Rules have narrowed the categories of fraud that can invoke fraud rules:

The tendered documents must be forged.

Two kinds of submitted documents are considered forged under the 2005 Rules: *first*, there are no documents at all, and the beneficiary creates all documents by himself; *second*, the information included in the documents presented to the bank is artificial.

Goods must fail to be delivered or there are no contracted goods.

This subsection might be considered to overlap the (i) provision, yet the 2005 Rules want to specify another aspect of fraud issues and suggest another allegation for the defrauded parties in court. By the same token, the 2005 Rules also want to emphasize that the standards of fraud rules are exceedingly high, which means only cases where there are no delivered goods at all or goods with entirely no value could call upon fraud rules under the 2005 Rules. In other words, it could be explained that if contracted goods are delivered with low quality or lack some units, it will not be deemed as fraud and parties cannot summon the fraud rules.

No actual sales agreement.

This provision is drafted to prevent the situation where the applicant and beneficiary cooperate to defraud the state-owned banks by using invalid contracts. By issuing this subsection, the 2005 Rules want to indicate that those who try to manipulate the banking system by using the invalid underlying contract and letters of credit will be suspended by the courts if their intentions are revealed. Concerning there are people always trying to manipulate the system (Int'l Chamber of Commerce, 1994, p. 9), and new types of fraud are not listed in subsections (i), (ii), or (iii), subsection (iv) is included. This subsection works as a security faucet to prevent any further dishonest behaviours in the future (Gao, 2007).

In 2016, the Provisions of the Supreme People's Court on Several Issues concerning the Trial of Disputes over Independent Guarantee (hereinafter referred to as "2016 Provisions") is adopted by the Judicial Committee of the Supreme People's Court and are valid on 01 December 2016. Even though the scope of this thesis is mainly focused on documentary credits, fraud standards listed in this Provisions which mainly focus on independent guarantee are still worth to be recognized under this part.

Article 12 of the 2016 Provisions stated that (Supreme People's Court of the People's Republic of China, 2016)[99]:

> "The people's court may determine that an independently guaranteed fraud is committed in any of the following circumstances:
> 1. The beneficiary makes up a false underlying transaction by colluding with the applicant or other people;
> 2. The third party's documents presented by the beneficiary are counterfeit or contain false information;
> 3. The debtor under the underlying transaction is deemed to be free of payment or indemnity liability by the court decision or arbitration award;
> 4. The beneficiary confirms that the debt obligation under the underlying transaction has been fulfilled in full or that the expiry-triggering event stated in the independent guarantee does not occur; and
> 5. Other circumstances where the beneficiary having no right to demand payment abuses such right on purpose."

The legislators also narrow the circumstances which can invoke fraud rules in the 2016 Provisions. Under the light of Article 12 of the 2016 Provisions, fraud standards are drafted quite similarly to Article 8 of the 2005 Rules. Both articles recognize the chances which the beneficiary colluding with the applicant to make up a false contract to defraud the national bank and ban it. Under Article 12, the forged documents presented under the independent guarantee are considered fraud and fraud rules shall be invoked (Supreme People's Court of the People's Republic of China, 2016).

However, based on the special features of the independent guarantee, subsections 3 and 4 of Article 12 are drafted differently from the 2005 Rules to prevent the debtor to defraud once he is determined to be free from his payment obligation in the underlying contract or in case the debt obligation is to fulfil, and the beneficiary confirms that or the situations which can trigger the termination do not happen. Subsection 5 is added to avoid further deceitful conducts (Supreme People's Court of the People's Republic of China, 2016).

Exemption of fraud rules

Having fraud rules embodied in domestic law is not only to protect the defrauded parties but also to save innocent parties. In other words, the fraud rules should not be invoked once the documents are tendered by innocent parties.

[99] The translation of *Provisions of the Supreme People's Court on Several Issues concerning Trial of Disputes over Independent Guarantee* is borrowed from the website of China International Commercial Court. *See more at*: http://cicc.court.gov.cn/html/1/219/199/201/783.html

Preserving the economic benefit of letters of credit is the main reason why fraud rules have regulations stating some parties are exempt from the rules of the fraud (Dolan, 1996). One benefit of using letters of credit is the beneficiary can receive money from a beneficiary's local bank. These banks are known as correspondent banks (Gao, 2007, p. 1080) which negotiate or purchase the documents that the beneficiary presented or take the right of proceeding with letters of credit under the name of warranty and providing loans to the beneficiary. When fraud is involved, innocent parties such as issuing bank, the applicant as well as aforementioned third parties will bear the loss. If such third parties are not protected, the economic benefits of letters of credit will be affected since there will be fewer local banks willing to take the risks as correspondent banks, which may lead to a reduction in the number of parties using this instrument. For these reasons, innocent third parties should be exempt from the exercise of fraud rules. Article 10 under the 2005 Rules[100] declares about the immune parties along these lines:

> "If the people's court maintains the occurrence of the letter of credit fraud, it shall make a ruling on suspending the payment or a judgment on terminating the payment under the letter of credit, except for any of the following circumstances:
> (i) The nominee or entrusting party of the issuing bank, in bona fide, has made the payment according to the instructions of the issuing bank;
> (ii) The issuing bank or the nominee or entrusting party thereof, in bona fide, has honored the instrument under the letter of credit;
> (iii) The confirming bank, in bona fide, has performed the payment obligation; or
> (iv) The negotiating bank, in bona fide, has negotiated the payment." (Supreme People's Court of the People's Republic of China, 2005)

Under this provision of the 2005 Rules, there are four circumstances to which fraud rules cannot be applied:

First, the courts cannot apply the fraud rules when a "nominated person" or authorized person has made their payment under "the instructions of the issuing bank" and requirements of the letter of credit (Supreme People's Court of the People's Republic of China, 2005). Under Article 12(b) of UCP 600 [101], the "nominated person" is similar to the "person authorized by the issuing bank", both are authorized by the issuer in letters of credit (International Chamber of Commerce, 2007).

Second, the Courts cannot apply fraud rules when the tendered documents are accepted by the "issuing bank or its nominated or authorized person" with good faith (Supreme People's Court of the People's Republic of China, 2005). This subsection shows a truly narrowed way to

[100] The English translation of *The Rules of the Supreme People's Court Concerning Several Issues in Hearing Letter of credit Cases* is borrowed from the translation of AsianLII. See more at: http://www.asianlii.org/cn/legis/cen/laws/potspcosicttocodoloc1163/

[101] Article 12(b) of UCP 600 provides:
By nominating a bank to accept a draft or incur a deferred payment undertaking, an issuing bank authorizes that nominated bank to prepay or purchase a draft accepted or a deferred payment undertaking incurred by that nominated bank.

exercise fraud rules under the 2005 Rules in P.R.C. As we may be aware, the time when the beneficiary is paid will be depended on the type of drafts along with the documents. It could be the time draft, the sight draft, or deferred payment obligation (Dole Jr., 2008, pp. 745- 746)[102] (Sandler & Ferrante, 1986, p. 614)[103] (Dolan, 1999, pp. 1035-1036) (McLaughlin, 1990, pp. 149, 155-156). Most beneficiaries want to receive their payment as soon as possible so letters of credit will provide the sight draft (Dolan, 1985, p. 18). In the situation with the sight draft in which the payment is made right after the conformed documents, there will be no chance for the applicant to stop the payments (Gao, 2007, p. 1081). When it comes to the time draft, the payment will be delayed for a certain time after the documents are presented. The issuing bank shall pay the beneficiary when the mature day arrives (Dolan, 2011, pp. 1269, 1272) or in case the letter of credit provides the deferred payment obligation, the beneficiary will be paid on a stated date (Dolan, 1999, pp. 1035-36, 1046)[104] (Dole Jr., 2008, pp. 737-738) (McLaughlin, 1990, pp. 155-156). In this case, fraud rules could be invoked if the tendered documents are accepted but no payment is made (Gao, 2007, p. 1081).

So, under subsection (ii) of Article 10 of the 2005 Rules, the chances to apply fraud rules are extremely limited because considering from the moment the documents are accepted with good faith, the payment cannot be suspended (Supreme People's Court of the People's Republic of China, 2005). To stop the payment, the applicant must apply for an injunction before the document is presented. According to Xiang Gao (Gao, 2007, p. 1082), this provision is "unfortunate" since all the parties holding the accepted documents will be exempt from the rules of fraud and this situation "obviously defeats the whole purpose of the fraud rules" (Gao, 2007, p. 1082).

Third, the Courts cannot apply fraud rules if the confirmer has paid the presenter with good faith. Normally, the beneficiary wants to receive advice and payment from a local bank, so the issuer will authorize a beneficiary's local bank to honour the documents, this local bank is called confirming bank. To the third-party presenter and the beneficiary, the confirming bank has an equal position comparing to the issuing bank because it gives bits of advice, accepts, and honours the documents (International Chamber of Commerce, 2007)[105]. With good faith, the confirmer either accepts or refuses to honour the presented documents when fraud is found. Hence, if the confirmer pays with good faith, they are protected by the 2005 Rules (Gao, 2007, p. 1082).

[102] The beneficiary will demand for the type of drafts under the letter of credit.
[103] The beneficiary will receive their payment right after they present the complied documents.
[104] The deferred payment obligation is also known as the "usance".
[105] Article 2 of UCP 600 provides:
A confirming bank undertakes to reimburse another nominated bank that has honored or negotiated a complying presentation and forwarded the documents to the confirming bank. Reimbursement for the amount of a complying presentation under a credit available by acceptance or deferred payment is due at maturity, whether or not another nominated bank prepaid or purchased before maturity. A confirming bank's undertaking to reimburse another nominated bank is independent of the confirming bank's undertaking to the beneficiary.

Fourth, the Courts cannot apply fraud rules when the negotiation bank has handled the letter of credit in good faith (Supreme People's Court of the People's Republic of China, 2005). Under Article 2 of UCP 600, negotiation "means the purchase by the nominated bank of drafts (drawn on a bank other than the nominated bank) and/or documents under a complying presentation, by advancing or agreeing to advance funds to the beneficiary on or before the banking day on which reimbursement is due to the nominated bank" (International Chamber of Commerce, 2007). Before the definition in UCP 600, in practice, there are several interpretations among the international bankers in the negotiation (Gao, 2007, p. 1082). In this way, in P.R.C., when bank claims that they are negotiation banks, they must present to the court proof that they have paid for documents (Gao, 2007, p. 1083).

As has been seen, all four subsections under Article 10 of the 2005 Rules mention "good faith" along with all processes of parties in the letter of credit. In the light of Article 10 of the 2005 Rules, good faith must be understood as "without notice of fraud" (Gao, 2007, p. 1083). In turn, under the guidance of Article 10 of 2005 Rules, when a negotiation bank honours the documents with good faith means that they do not have any awareness of fraud in the transactions, and with that explanation, they can be exempt from fraud rules. Consequently, once the negotiation bank notices fraud included in the transactions but still negotiates the documents, then the negotiation bank should not be protected.

However, this definition of good faith could not be applied when it comes to the confirming bank. The confirmer is in the same spot as the issuer from the perspective of the beneficiary and the third-party presenter, he must honour the tendered documents if the documents on their face comply with the requirements under the letter of credit as Article 2 of UCP 600 has stated so (International Chamber of Commerce, 2007). The negotiation bank, on the contrary, still can refuse to negotiate and honour the documents of the beneficiary because they are not bound to pay once fraud is involved in the contract or in the letter of credit. But things are different to the confirming bank. If the confirming bank turns the presented documents down because there are frauds within the transactions, they might find themselves being dragged into litigations by the presenter. Accordingly, if the confirmer chooses to honour the documents presented on their face conforming to the requirements of the letter of credit even though fraud is involved and they notice it, the confirming bank must be secured by the fraud rules because of its extraordinary condition. So, in this circumstance, "good faith" cannot be defined as "without notice of fraud" but "without collusion" with the fraudster (Gao, 2007, p. 1083).

The Remedies of The Courts

Under the light of Article 9 of the 2005 Rules:

> "The applicant, the issuing bank or any other interested party may apply to a competent people's court for a ruling to suspend the payment under the letter of credit if they have found out that the circumstances [of fraud] set out in Article 8… have happened and will cause them irreparable damage." (Supreme People's Court of the People's Republic of China, 2005)

This definition of Article 9 is based on Article 93 and Article 94 of the CPL of PRC but it is not indistinguishable since, within the CPL of PRC, the interested party could apply to a People's Court for "property preservation" which will be acted as "sealing up, confiscation, the freezing of assets" (China People's Congress, 1991).

Under the regulations in the CPL of PRC, the applicant can bring the case to the court to ask for an assets-frozen decision, however, this action could not stop the other party continues to abuse the applicant's interest. In the CPL of PRC, there was no injunction or restraining order which is similar to the common law, this circumstance led to the abuse of the process of the letter of credit in the past in P.R.C when the applicant tried to postpone the payment process and the court could only grant decisions which freeze the assets of related parties (Gao, 2007, p. 1083). This also creates several problems with the foreign banks because they argued that they must be paid once they honour the documents with good faith.

Article 9 of the 2005 Rules had filled the gap since the courts now can grant a restraining order or an injunctive relief without freezing assets. Under Article 15 of the 2005 Rules, "In case the people's court, through substantial trial, determines that a letter of credit fraud is constituted and that none of the circumstances as prescribed in Article 10 of these Provisions exists, it shall make a judgment on terminating the payment under the letter of credit." (Supreme People's Court of the People's Republic of China, 2005), this regulation means that the courts could also grant other kinds of remedies in case fraud rules are invoked. This remedy is nonetheless usable once the trial court is complete, there are no innocent parties, and fraud is established, the court can issue a permanent postponement on the payment process under the letter of credit.

Hence, there are two kinds of remedies available under the 2005 Rule which is

- Ruling to postpone the payment, which is a temporary measure before investigating the case
- Permanently stop the payment, which is only available after a full trial court.

Parties applying for Court remedies

Under Article 9 of 2005 Rules[106], "If the applicant, **issuing bank** or any other interested party finds any of the circumstances as prescribed in Article 8 of these Provisions, and believes that irremediable losses will be caused to it, it may file an application with the competent people's court for suspending the payment under the letter of credit." (Supreme People's Court of the People's Republic of China, 2005). Once fraud is found in the transactions, the applicant as the party standing in the priority position could take legal action and asks the courts for injunctive relief. The issuing bank is also listed as one of the parties applying for court remedies under

[106] The English translation of *The Rules of the Supreme People's court Concerning Several Issues in Hearing Letter of credit Cases* is borrowed from the translation of AsianLII. See more at: http://www.asianlii.org/cn/legis/cen/laws/potspcosicttocodoloc1163/.

Article 9, however, according to Xiang Gao (2007), this is simply strange and illogical. Normally, international practice and rules allow the issuer continues to honour the documents if they conform to the requirements of the letter of credit. Once fraud is found, the issuer can refuse to do so. And it is much more economical for the issuing bank to just turn the documents down than to go to court to ask for an injunction. Surprisingly, Chinese banks have a different view about this provision because they support this provision. According to Xiang Gao, the reason behind this encouragement is that the banks are afraid of their reputation in international trade. Their reputation will be affected if they refuse to honour documents because of fraud. It would be better for their statures if they reject the documents not by themselves but by courts' judgments (Gao, 2007, p. 1085).

The Jurisdiction

As illustrated above, the applicant or the issuing bank, or any third party who has relations with the creditor can ask the court for a ruling under Article 9 of 2005 Rules (Supreme People's Court of the People's Republic of China, 2005). In P.R.C., letters of credit are considered financial instruments having foreign elements. The competent court could be selected under Article 4 of the *Provisions of the Supreme People's Court on Several Issues Regarding the Establishment of the International Commercial Court* as follows [107]: "Judges of the International Commercial Court shall be selected and appointed by the Supreme People's Court from the senior judges who are experienced in trial work, familiar with international treaties, international usages, and international trade and investment practices, and capable of using Chinese and English proficiently as working languages." (Supreme People's Court of Peolpe's Republic of China, 2018).

The requirements for the remedies

The acceptance of the people's courts to the application to postpone the payment process under a letter of credit is declared in Article 11 of the 2005 Rules[108] as follows:

> "Where a party concerned files an application for suspending the payment under the letter of credit before it initiates legal proceedings, and if the following conditions are met, the people's court shall accept the application:
> (i) The people's court that accepts the application has the jurisdiction over the case of dispute over the letter of credit;
> (ii) The evidential materials presented by the applicant prove the existence of any of the circumstances as prescribed in Article 8 of these Provisions;

[107] The English translation of *Provisions of the Supreme People's Court on Several Issues Regarding the Establishment of the International Commercial Court* is borrowed from the website of Supreme People's Court of the People's Republic of China. See more at: http://english.court.gov.cn/2021-10/19/content_37548523.htm.
[108] The English translation of *The Rules of the Supreme People's court Concerning Several Issues in Hearing Letter of credit Cases* is borrowed from the translation of AsianLII. See more at: http://www.asianlii.org/cn/legis/cen/laws/potspcosicttocodoloc1163/.

(iii) If no measure is taken to suspend the payment under the letter of credit, the legitimate rights and interests of the applicant will be damaged beyond remedy;
(iv) A reliable and full guarantee has been provided by the applicant; and
(v) None of the circumstances as mentioned in Article 10 of these Provisions exists.
A party concerned shall satisfy the conditions as prescribed in Items (2) through (5) of the preceding paragraph if it, in the court action, applies for suspending the payment under the letter of credit." (Supreme People's Court of the People's Republic of China, 2005)

Article 11 of the 2005 Rules was mainly drafted based on the CPL of PRC 1991 (Gao, 2007, p. 1084). The court could grant injunctive relief for the applicant once these conditions mentioned above are met and the payment under a letter of credit shall be postponed. As has been mentioned, subsection (i) and (v) was discussed before, so within this part, the author will only declare subsection (ii), (ii), and (iv).

In this article, it is noticeable that the applicant must be well prepared for their application to the court and attaches it with adequate pieces of evidence about the established fraud. This adequate evidence is listed under Article 8 of the 2005 Rules (Supreme People's Court of the People's Republic of China, 2005). According to Xiang Gao, the Chinese court barely accepts a mere oral allegation about fraud, the claim must be in written forms (Gao, 2007, p. 1086).

Another condition to applying fraud rules is the damage that the applicant must handle. The applicant must prove that they will suffer irreparable damage created by the fraud under Article 11 of the 2005 Rules (Supreme People's Court of the People's Republic of China, 2005). Since the nature of letters of credit is truly special, the payment of letters of credit must be maintained and should not be interrupted under any circumstances, however, fraud rules are its exception so the court must be very careful in interfering with the payment process and must consider fraud rules as the last solution.

Article 11(iv) of the 2005 Rules declares that if the applicant invokes the fraud rules under the credit, they should maintain an "effective and adequate security" (Gao, 2007, p. 1087). As demonstrated above, the 2005 Rules adopt the view that security must be given to make sure that the damage from the other parties shall be applied to compensate once the action was taken improperly.

The Ruling of the Courts after receiving the application

Upon the definition under Article 12 of the 2005 Rules, it takes a maximum of 48 hours for the people's court to declare a ruling to infer the process under a letter of credit.

"The people's court should make a ruling within 48 hours after accepting the application for suspending the payment under the letter of credit. Such a ruling, if made by the people's court, shall be executed at once."

As has been seen, the courts, under Article 12, must act promptly once the applicants submit their applications. This regulation indicates the "practical requirement for the dealing of a case of a letter of credit fraud" (Gao, 2007, p. 1088). The financial benefit of letters of credit might be affected once the courts do not take the application quickly and save the issuer from being dragged into a more difficult circumstance. The international reputation of the issuer might be harmed if they refuse to pay the beneficiary who may not be the fraudster as the claim of the applicant, or their name will be affected once the beneficiary is truly the fraudster. Furthermore, Article 12 states that:

> "The people's court shall state the applicant, the party against whom the application is filed and the third party in the ruling on suspending the payment under the letter of credit." (Supreme People's Court of the People's Republic of China, 2005)

The procedure in P.R.C is a little bit different from the common law procedure regarding the letter of credit law. In the common law, the applicant will take legal actions to prevent the issuing bank from paying or asking for injunctive relief to avoid the beneficiary from receiving payment. In P.R.C., when the applicant takes a claim to the court that fraud is engaged in the transactions, the court can suspend the payment using the account in the bank of the applicant and the applicant should note the issuer and confirmer as third party. This conduct is considered a property preservation measure under the guidance of the CPL (China People's Congress, 1991). Article 14 of the 2005 Rules further states that:

> "In the course of hearing a letter-of-credit fraud case, the people's court may, where necessary, put-on trial the dispute over letter of credit together with the dispute over the basic transaction." (Supreme People's Court of the People's Republic of China, 2005)

The procedure described in the 2005 Rules is similar to the procedure in the CPL, the only difference between these two is the applicant can require the court to make a temporary injunction to interfere with the payment rather than freezing the assets of the banks.

Reconsideration for The Ruling of The Court

If a party finds the court's ruling is improper, they can apply to a higher People's Court within 10 days upon the delivery of the ruling under Article 13 of the 2005 Rules

> "Where a party concerned has any objections to the ruling made by the people's court on suspending the payment under the letter of credit, it may apply for reconsideration to the people's court at the next higher level within 10 days from the day when the ruling is served. The people's court at the next higher level shall make a ruling within 10 days as of the date of receipt of the reconsideration application.
> The original ruling shall not be suspended from execution during the period of reconsideration." (Supreme People's Court of the People's Republic of China, 2005)

This article is drafted based on Article 99[109] of the CPL of P.R.C 1991 (China People's Congress, 1991), however, there are some modifications to fit with letters of credit's special nature. Under Article 13, those who are not satisfied and have an objection to the decision of the court can apply their appeal to the next higher-level court for reconsideration of the judgment within 10 days.

The level of the courts is raised under this Article while they handle the cases relating to fraud in letters of credit and this regulation clearly expresses the consideration of the exception of the independent principle of letters of credit. Article 13 of the 2005 Rules demands a ruling must be issued by the court if the applicant submits a reconsideration to the court. According to Xiang Gao, "this is more formal than a resolution under Chinese law" (Gao, 2007, p. 1089).

[109] Article 99 of the CPL of P.R.C 1991 provides:
If the party concerned is not satisfied with the order made on property preservation or execution, he may apply for reconsideration which could be granted only once. Execution of the order shall not be suspended during the time of reconsideration.
Article 99 of the CPL of P.R.C 1991 is replaced by Article 108 of CPL of P.R.C 2017. Article 108 provides:
If a party is dissatisfied with a ruling for preservation of property or preliminary execution, he may apply once for review. Execution of the ruling shall not be suspended during the period of review.
As has been stated, the author shall only focus on the CPL of P.R.C 1991 even though it is expired.

CHAPTER VIII

THE VIETNAM LETTER OF CREDIT LAW AND FRAUD RULES

One of the most serious issues in defining fraud rules is to ensure commercial utility by retaining the independent principle of the letter of credit law. The definition of fraud rules is also very important because standards for fraud rules are quite complex. If we set the standards too high, fraud rules would lose their effectiveness. If the standards are too low, the applicant may use the rules of fraud as a method to violate letters of credit by stopping the payment from the issuer to the beneficiary. It is still a long way to go for the Vietnamese legal system to implement the fraud rules into domestic law. The legislators need to consider international legal sources such as the UCP and the UN Convention 1995 as well as approach other domestic laws or uniform codes of other countries such as the United States or the People's Republic of China. The documentary credits law including the independent principle and rules of fraud may have an even greater effect in Vietnam because Vietnam is a civil law country and civil countries normally count on statuses rather than cases.

In this chapter, the author will investigate and explain the law of letters of credit at the early age of the Vietnamese legal system. Then the author will consider the situation in Vietnam by giving an opinion about the typical case law published by Vietnam Supreme Court.

8.1. International Trading in Vietnam in its early stages

The banking activities in Vietnam first started in 1875 with the first establishment of the first branch of the Banque de l'Indochine in Saigon city (now known as Hochiminh City). The bank worked as a commercial bank as well as issuing currency in Cochinchina and the French Indies (Pilon & Weiler, 2011, p. 97). The Banque de l'Indochine was considered a colonial bank that managed the colonial properties in South-East Asia of the French Government. Credit activities in international payment, even listed, were very limited.

After the success of the August Revolution in 1945, six years later, on 5 May 1951, the National Bank of Vietnam (now known as the State Bank of Vietnam) was set up. In its early years, due to being in a period of the resistance war against France, there was no international payment. Afterwards, the economy of Vietnam began to recover and developed, the North of Vietnam tried to establish economic relations with foreign countries (mainly socialist countries), focusing mostly on money transfers.

In 1963, the Bank for Foreign Trade of Vietnam was set up on 1st April by the Foreign Exchange Bureau (of the State Bank of Vietnam) (Vietcombank, 2019), now known as the Joint Stock Commercial Bank for Foreign Trade of Vietnam (hereinafter referred to as "Vietcombank") was established in the North. Its functions were specified in developing international banking activities. In the South of Vietnam from 1954 to 1975, there was no information about international trading using any international payment mechanism. From

1975 to 1989, there were several embargoes on Vietnam. Most of the international economic activities were trading with the socialist states and were conducted by the State Bank of Vietnam. At Sixth Party Congress, a resolution was adopted based on the situation in Vietnam at that time (known as the "Doi Moi" plan in 1986). As a result, since 1990, the international business economy had been grown dramatically.

8.2. The Regulations govern Letters of Credit in the Vietnamese Legal System

The economic reformation, "Doi Moi", has created new platforms for international trade and consequently, the transactions between Vietnamese entrepreneurs and foreign partners have increased dramatically. Because of this, payments using letters of credit also become more popular among Vietnamese entrepreneurs. Yet, the legal literature in Vietnam barely mentions the law of letters of credit and only admits the Uniform Customs and Practice as a "de facto law" (The National Assembly, 2005). The author analysed all laws and by-law documents which mention the letter of credit in Vietnam's legal system. However, some of them are expired and until now, there are no laws directly mentioning the law of letters of credit.

Ordinance No. 28/2008/PL-UBTVQH11 dated 13 December 2005 on Foreign Exchange Control (hereinafter referred to as "Ordinance No. 28/2008/PL-UBTVQH11") and Ordinance No. 06/2013/UBTVQH13 dated 18 March 2013 on Amending and Supplementing several articles of the Ordinance on Foreign Exchange Control (hereinafter referred to as "Ordinance No. 06/2013/UBTVQH13").

The process of international letters of credit was not mentioned in these two Ordinances. However, since the beneficiary in international transactions was usually a foreign partner, the bank must comply with the provisions of Ordinance No. 28/2008/PL-UBTVQH11 and other substantial law documents.

Decree No. 101/2012/NĐ-CP dated 22 November 2012 on Non-cash Payments (hereinafter referred to as "Decree No. 101/2012/NĐ-CP")

Under Article 1 of Decree No. 101/2012/NĐ-CP, this Degree deals with non-cash payments, including "opening and using payment accounts, non-cash payment services, payment intermediary services, organizing, managing, and supervising the payment systems" (The Government, 2012). The subjects of application are described in Article 2 as "(1) Providers of non-cash payment services (2) Providers of payment intermediary services and (3) Users of non-cash payment services and payment intermediary services" (The Government, 2012). Letters of credit are still not directly mentioned in this Decree; however, this Decree is drafted to deal with non-cash payments, which makes it become a reference for letters of credit in Vietnam.

Decision 226/2002/QD-NHNN dated 26 March 2002 on the Issuance of The Regulation on Payment Activities Through Payment Service Suppliers (hereinafter referred to as "Decision 226/2002/QD-NHNN")

Article 16 of the Decision 226/2002/QD-NHNN stated that:

> "1. Letter of credit shall be a conditional written undertaking opened by banks at the request of a payment service user (the applicant for opening the letter of credit), under which, banks shall perform the requests of the payment service users (the applicant for opening letter of credit) to:
> - Effect the payment or authorize other banks to effect the payment immediately at the instruction of the payee upon receipt of a set of presented documents satisfying the conditions of the letter of credit; or
> - Accept to make the payment or authorize other banks to make the payment at the instruction of the payee at a specific future time upon receipt of a set of presented documents satisfying the conditions of the letter of credit.
> 2. The opening, issuance, amendment, notification, confirmation, examination of the payment documents and rights, responsibilities, etc. of related parties in payment by letter of credit shall be applicable upon the agreement of parties engaging in the payment and in accordance with current applicable laws of Vietnam."

This Decision mentioned letters of credit in Article 16 and the definition of the letter of credit payment was explained to fit with the characterization in the UCP 600. It defined and mentioned only two ways of payment (1) payment immediately and (2) payment at the instruction at a specific future time as followed. Unfortunately, Decision 226/2002/QD-NHNN was expired and replaced by a new by-law document.

Circular No. 46/2014/TT-NHNN dated 31 December 2012 on the Guidelines for Non-Cash Payment Services (hereinafter referred to as "Circular 46/2014/TT-NHNN")

This Circular is a replacement for Decision No. 226/2002/QD-NHNN and the Decision No. 1092/2002/QĐ-NHNN dated 08 October 2002 of the Governor of the State Bank on promulgating regulations on procedures for payment made by payment service providers.

However, in Circular 46/2014/TT-NHNN, the Government removes the whole Article 16 of Decision 226/2002/QD-NHNN and replaces it with the new definition in Article 3.3.6, which is "cash payment service" (State Bank of Vietnam, 2014) and explains the term as " Regarding payment services, the payment service provider shall comply with the sender's request specified in the agreement between the payment service provider and the sender and by relevant regulations of law" under Article 10.2 (State Bank of Vietnam, 2014).

Circular 46/2014/TT-NHNN governs the payment procedures through payment service-providing organizations. It guides the order of making, controlling, circulating, processing documents, and accounting domestic payment transactions through payment service-providing organizations in Vietnam. The procedures relating to the opening and payment of letters of credit for domestic payments are stated in this Circular. Although these regulations do not

apply to international letters of credit, they can be considered an important source of reference when developing specific legal provisions for letters of credit and its fraud rules of Vietnam.

Decision No 711/2001/QD-NHNN dated 25th May 2001 on Promulgating The Regulation on the Opening of Letter of Credit for Importing Goods with Deferred Payment and Decision No. 1233/2001/QD-NHNN dated 26th September 2001 on the Amendment of Article 15 of the Regulation on Opening of Deferred Letter of Credit for goods import issued in conjunction with the decision No. 711/2001/QD-NHNN dated 25th May 2001

Both Decisions expired on October 20, 2012, and there are no other by-law documents to replace them, however, it is worth noting Article 2 which described the issuing and interests of deferred letters of credit for imported goods.

> "Banks that perform deferred payment L/C operation include the State commercial banks, investment banks, development banks, joint stock commercial banks, policy banks, joint-venture banks, branches of foreign banks in Vietnam, and banks of other types (hereinafter called "banks"), […]"

Both Decisions did not include various types of letters of credit, however, they are still considered important sources.

Law on Negotiable Instruments dated 29 November 2005

Under Article 3.2 of Law on Negotiable Instruments dated 29 November 2005 issued by the National Assembly (hereinafter referred to as "Law on Negotiable Instruments 2005"), the independent principle is recognized as follows:

> "The negotiable instrument relationships stipulated in this Law are independent and are not dependent on a transaction which is the basis for issuance of a negotiable instrument stipulated in clause 1 of this article"

The Law on Negotiable Instruments 2005 acknowledges independent principle, one of the main rules in the letter of credit, however, it still does not govern letters of credit because its governing scope is negotiable instruments in Article 1 including "bills of exchange, promissory notes, cheques, and other negotiable instruments, excluding long-term negotiable instruments issued by organizations aimed at raising capital on the market" (The National Assembly, 2005). Under the light of Article 6 of the Law on Negotiable Instrument 2005, in the case of "negotiable instrument relationships involving foreign elements, the parties to the negotiable instrument relationship may agree to apply international commercial practices" (The National Assembly, 2005) such as International Chamber of Commerce's Rules on Uniform Customs and Practice for documentary credits. Hence, it means that the Vietnamese legal system allows transactions in Vietnam that contain foreign elements to be governed by UCP. The current law system of Vietnam does not have specific provisions for letters of credit so once a dispute happens between Vietnam merchants and their foreign partners related to fraud, the Courts or

Arbitrations usually refer to the general provisions of the Civil Code, the Civil Procedure Code, the Commercial Law, and other by-law documents. The Vietnam People's Courts could make the same mistakes as the courts in China in its early years without specific legislation[110] and such situations might harm the reputations of the Vietnamese banks in international trade.

Law on Credit Institutions dated 16th June 2010 (hereinafter referred to as "Law on credit institutions 2010")

Under the guidance from Official Document No. 1606/TCT-DNL dated 22 April 2020 of the General Department of Taxation (hereinafter referred to as "Official Document"), letters of credit are considered payment services due to the quotation from Article 4.15 of Law on Credit Institutions 2010:

> "Provision of payment services through account means provision of payment facilities; payment of cheques, payment orders, receipt order, bank cards, LCs and other payment services through a customer's account" (Vietnam National Assembly, 2010).

The goal of this Official Document is to announce that the letter of credit is not subject to VAT ("added-value tax"). It is the latest source of the Vietnamese legal system that mentioned letters of credit. Under the perception of the Law on Credit Institutions 2010, it is recognized that the letter of credit is being used in Vietnam as a provider of payment services, however, other aspects of letters of credit are not mentioned such as fraud rules.

8.3. Case Law No. 13/2017/AL

The Vietnam legal system has not included the provisions regarding the fraud exception in letters of credit, which may lead to several problems. In some circumstances, the applicant might try to take advantage of this loophole and use the courts' injunctions to prevent the payment obligation happen whether fraud is invoked or not. The courts with a shortage of regulation regarding the fraud rules of letters of credit shall depend on the Civil Code to issue judgments that might favour the applicant. Such judgments shall get critics from letters from credit experts and banks. Case Law No. 13/2017/AL is listed in the Supreme People's Court of Vietnam's set of cases law has shown the relation to the legality of letters of credit when the underlying contract is cancelled in international trade. Even though this case law does not fully capture the state of affairs in Vietnam and cannot serve as the foundation for a scientifically rigorous analysis of the gaps in Vietnam's letter of credit law, it is still crucial because the Vietnam People's Supreme Court has not yet issued a specific ruling on the fraud problem in letters of credit. Because of this, the decisions made by the Vietnam People's Supreme Court in this particular case significantly impact subsequent decisions made by lower courts. As a result, an analysis is valuable.

[110] See Chapter VII.7.5.1. for further information about the situations of Chinese banks in the early years.

The 2005 Rules of the PRC and Section 5-109 of UCC are important sources of letter of credit law relating to the fraud exception that merits consideration, especially the 2005 Rules because of the similarity between the legal systems in Vietnam and China. In general, the UCP provisions will have a bigger influence on situations involving non-fraud, whereas the 2005 Rules of PRC and Section 5-109 of UCC explicitly provided for the letter of credit law's fraud exemption. Therefore, a significant source for the examination of Case Law No. 13/2017/AL is the fraud regulations of the 2005 Rules and Section 5-109 of UCC.

8.3.1. The Judicial System in Vietnam

Before going into the case, it is necessary to have a brief introduction to Vietnam's judicial system.[111] The two-tier system is applied in the Vietnam People's Court system, which consists of the courts of first- instance and the courts of appeal[112]. Further reviews for the judgments could be conducted in case of special circumstances[113]. Adhering to the tradition of civil law and Article 5 of the Law on Organization of People's Court 2014, the Vietnamese courts carry their judgments independently[114] (The National Assembly, 2014).

The judges will be appointed by the Chief Justice of the Supreme People's Court under Article 7 of the Law on the organization of the People's Court 2014[115] (The National Assembly, 2014). The budget of the local courts will be decided by the National Assembly considering Article 96 (The National Assembly, 2014)[116]. These conducts are proving the efforts to separate the courts from the local government.

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[111] The English translation of the Law on Organization of People's Court 2014 is borrowed from the translation of the website thuvienphapluat.vn. See the original version at: https://thuvienphapluat.vn/van-ban/Bo-may-hanh-chinh/Luat-to-chuc-Toa-an-nhan-dan-2014-259724.aspx.

[112] This system is stated in Article 6.1 of the Law on Organization of People's Court 2014 as followed:
"1. The first instance and appellate trial system shall be guaranteed.
First-instance judgments and decisions of courts may be appealed or protested against in accordance with procedural law. First-instance judgments and decisions that are not appealed or protested against within the time limit prescribed by law shall take legal effect.
Cases in which first-instance judgments or decisions are appealed or protested against shall be brought to the appellate trial. Appellate judgments and decisions of courts shall take legal effect."

[113] Article 6.2 of the Law on Organization of People's Court 2014 provides:
"2. In case a violation of law is detected in a legally effective judgment or decision of a court, or a new circumstance arises as prescribed by the procedural law, such judgment or decision shall be re-considered according to cassation or reopening procedures."

[114] Article 5 of the Law on Organization of People's Court 2014 provides: "People's courts shall be independently organized based on their jurisdiction."

[115] Article 7 of the Law on the organization of the People's Court 2014 provides:
"Appointment of judges, election, or nomination of assessors:
1. The appointment of judges is applicable to courts.
2. The election of people's assessors is applicable to people's courts of provinces and central-affiliated cities, and people's courts of rural districts, urban districts, towns, provincial cities, and the equivalent. The nomination of army men's assessors is applicable to military courts of military zones and the equivalent and to regional military courts."

[116] Article 96 of the Law on Organization of People's Court 2014 provides:
"Operation funds of people's courts
1. Operation funds of the Supreme People's Court, superior people's courts, people's courts of provinces, centrally run cities, rural districts, urban districts, towns, provincial cities, and the equivalent shall be submitted by the Government to the National Assembly for decision after reaching agreement with the Supreme People's Court. In case the Government and the Supreme People's Court cannot reach agreement on estimated operation funds of

Vietnam's case law is not widely published and access to the judgments is difficult. However, in 2015, several trial decisions and judgments were chosen by the Council of Justice of the Supreme People's Court to be formed as judicial case law. The case law then can be published to the judges to adjudicate their judgments. The Resolution 04/2019/NQ-HDTP dated 18 June 2019 on Process for Selecting, Publishing and Applying Precedents requires "the judges and the lay judges must study and apply the precedent to settle similar cases so that the two cases had similar facts to one another shall have the same settlement results. If the precedent is not applied in a case with similar facts, the Courts must explain the judgment" (Council of Justice of Supreme People's Court, 2019)[117]. The Chief Justice of the Supreme People's Court has approved and published 39 cases law on trade law, civil law, and so on (Supreme People's Court, 2017). This is the first set of case law that the Supreme People's Court has published even though based on traditional civil law, it is an old concept.

Case Law 13/2017/AL which shall be mentioned in this thesis is published in this first set of case law and was first resolved by the Hochiminh People's Court. To explain why Hochiminh People's Court has the first authority to resolve this case, it is necessary to have a brief introduction to the procedure for the settlement of civil cases involving foreign elements in Vietnam. Case Law 13/2017/AL was decided that it involved foreign elements due to Article 405.2 of the Code of Civil Procedure 2004[118] as follow:

> "A civil case or matter involving foreign elements means a civil case or matter where at least one of the involved parties is a foreigner or an overseas Vietnamese; or civil relations between the involved parties being Vietnamese citizens, agencies or organizations but the bases for establishing, changing or terminating such relations comply with foreign laws, have arisen overseas or assets involved in such relations are located overseas."[119]

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people's courts, the Chief Justice of the Supreme People's Court shall propose the National Assembly to consider and decide on such funds.
2. Operation funds of military courts shall be estimated by the Ministry of National Defense in coordination with the Supreme People's Court before proposing the Government submit them to the National Assembly for decision.
3. The management, division, allocation, and use of operation funds must comply with the Law on the State Budget and other relevant laws.
4. The State shall prioritize investment in physical foundations and development of information technology for people's courts."

[117] The English translation of Resolution 04/2019/NQ-HDTP is borrowed from the translation at the website thuvienphapluat.vn. See the original version at: https://thuvienphapluat.vn/van-ban/Thu-tuc-To-tung/Nghi-quyet-04-2019-NQ-HDTP-ve-quy-trinh-lua-chon-cong-bo-va-ap-dung-an-le-293168.aspx

[118] The English translation of the Code of Civil Procedure of Vietnam 2004 is borrowed from the translation at the website thuvienphapluat.vn. See the original version at: https://thuvienphapluat.vn/van-ban/Thu-tuc-To-tung/Bo-luat-To-tung-dan-su-2004-24-2004-QH11-52189.aspx.

[119] By the time this judgement is issued, the Code of Civil Procedure of Vietnam 2004 was valid. However, Article 405.2 of the Code of Civil Procedure of Vietnam 2004 is now replaced by Article 464.2 of the Code of Civil Procedure of Vietnam 2015. The Article 464.2 of the Code of Civil Procedure of Vietnam 2015 provides:
"2. A civil case involving foreign elements means a civil case falling in any of the following cases:
a) At least one party is a foreign individual/agency/organization;
b) All parties are Vietnamese citizens/agencies/organizations, but the relationship is established, changed, developed or broken up in a foreign country;

And the People's Court of Vietnam shall have jurisdiction to resolve this case considering Article 410.2.d of the Code of Civil Procedure 2004 as follows:

> "2. Vietnamese courts shall settle civil cases and/or matters involving foreign elements in the following cases:
> a) The defendant is a foreign agency or organization, which is headquartered in Vietnam, or the defendant has a managing agency, branch or representative office in Vietnam;
> b) The defendant is a foreign national or stateless person who permanently resides, works or lives in Vietnam or has assets in the Vietnamese territory;
> c) The plaintiff is a foreign national or stateless person who permanently resides, works or lives in Vietnam, for civil cases or matters claiming alimonies or parent identification;
> d) Civil cases or matters related to civil relations which are established, changed or terminated on the grounds prescribed by Vietnamese law, or which happen in the Vietnamese territory but involve at least one party being foreign individual, agency or organization.
> e) Civil cases or matters related to civil relations which are established, changed or terminated on the grounds prescribed by foreign laws or which happen in foreign countries, but involve all parties being Vietnamese citizens, agencies or organizations and either the plaintiff or the defendant resides in Vietnam;
> f) The disputes arise out of a contract with the partial or full performance thereof taking place in the Vietnamese territory;
> g) The divorce cases with the plaintiffs or the defendants being Vietnamese citizens."[120]

According to Article 3 of Law on Organization of People's Court 2014, the organization of Vietnam People's Courts is listed as follows:

> "1. The Supreme People's Court.
> 2. Superior People's Courts.
> 3. Courts of provinces and central-affiliated cities.
> 4. Courts of rural districts, urban districts, towns, provincial cities, and the equivalent.
> 5. Military courts."

The People's Courts of rural districts, urban districts, provincial capitals, provincial towns (hereinafter referred collectively to as "District-level People's Courts") shall have the jurisdiction to settle first-instance procedures with business dispute involving foreign element according to Article 33.1.b of the Code of Civil Procedure 2004[121]. However, because the

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c) All parties are Vietnamese citizens, agencies, and organizations but the parties of such civil relationship are overseas."
The English translation of the Code of Civil Procedure of Vietnam 2015 is borrowed from the translation at the website thuvienphapluat.vn. See the original version at: https://thuvienphapluat.vn/van-ban/Thu-tuc-To-tung/Bo-luat-to-tung-dan-su-2015-296861.aspx.

[120] Article 410.2 of the Code of Civil Procedure of Vietnam 2004 is now replaced by Article 469 of the Code of Civil Procedure of Vietnam 2015. The language in Article 469 of the Code of Civil Procedure of Vietnam 2015 remains the same as Article 410.2 of the Code of Civil Procedure of Vietnam 2004.

[121] Article 33 of the Code of Civil Procedure 2004 provides:

dispute in Case Law 13/2017/AL is a business dispute which "involves parties or properties in foreign countries or which must be judicially entrusted to Vietnamese consulates overseas or to foreign courts", hence, Case Law 13/2017/AL "shall not fall under the jurisdiction of the district-level People's Courts" according to Article 33.3 of Code of Civil Procedure 2004[122]. So, according to Article 34.1.c of Code of Civil Procedure 2004[123], this case law shall be resolved under the jurisdiction of the People's Courts of Provinces or Central-affiliated Cities. Case Law 13/2017/AL does not mention where Company A's headquarter is located, however, the author supposes that Company A's headquater is at Hochiminh city since they submit their allegation at the people's court in Hochiminh city according to Article 35.2.dd of Code of Civil

"Jurisdiction of the people's courts of rural districts, urban districts, provincial capitals, provincial towns
1. The people's courts of rural districts, urban districts, provincial capitals, and provincial towns (hereinafter referred collectively to as district-level people's courts) shall have the jurisdiction to settle according to first-instance procedures the following disputes:
a) Civil disputes over marriage and family, prescribed in Articles 25 and 27 of this Code;
b) Business, and trade disputes prescribed at Points a, b, c, d, e, f, g, h and i of Clause 1, Article 29 of this Code;
c) Labor disputes prescribed in Clause 1, Article 31 of this Code.
2. The district-level people's courts shall have the jurisdiction to resolve the following requests:
a) Civil requests prescribed in Clauses 1, 2, 3 and 4 of Article 26 of this Code;
b) Marriage and family-related requests prescribed in Clauses 1, 2, 3, 4 and 5 of Article 28 of this Code.
3. Disputes and requests prescribed in Clauses 1 and 2 of this Article, which involve parties or properties in foreign countries, or which must be judicially entrusted to Vietnamese consulates overseas or to foreign courts, shall not fall under the jurisdiction of the district-level people's courts."

[122] Article 33 of the Code of Civil Procedure 2004 is now replaced by Article 35 of the Code of Civil Procedure of Vietnam 2015. Article 35 of the Code of Civil Procedure of Vietnam 2015 provides:
"Jurisdiction of People's Courts of districts
1. People's Courts of districts shall have the jurisdiction to settle according to first-instance procedures the following disputes:
a) Disputes over civil matters, marriage and family, prescribed in Articles 26 and 28 of this Code;
b) Disputes over business/trade activities prescribed in clause 1 Article 30 of this Code;
c) Labor disputes prescribed in Article 32 of this Code.
2. People's Courts shall have the jurisdiction to resolve the following petitions:
a) Civil petitions prescribed in Clauses 1, 2, 3, 4, 6, 7, 8, 9 and 10 of Article 27 of this Code;
b) Petitions relating to marriage and family prescribed in Clauses 1, 2, 3, 4, 5, 6, 7, 8, 10 and 11 of Article 29 of this Code;
c) Petitions relating to business/trade activities prescribed in clause 1 and clause 6 Article 30 of this Code;
d) Labor petitions prescribed in clause 1 and clause 5 Article 33 of this Code.
3. Disputes and petitions prescribed in Clauses 1 and 2 of this Article, which involve parties or properties in foreign countries or which must be judicially entrusted to representative agencies of the Socialist Republic of Vietnam overseas or to foreign courts/competent agencies, shall not fall under the jurisdiction of people's Courts of districts, except for cases specified in clause 4 of this Article.
4. People's Courts of districts where Vietnamese citizens reside shall be in charge of cancelling illegal marriage, settling divorce petitions and disputes pertaining to rights and obligations of spouses, parents and children, parents and children adoption and guardian relationship between Vietnamese citizens living in frontier areas and citizens of neighboring countries living near Vietnam according to provisions of this Code and other Vietnam's law provisions."

[123] Article 34.1 of the Code of Civil Procedure 2004 is now replaced by Article 37.1 of the Code of Civil Procedure of Vietnam 2015. Article 37.1 of the Code of Civil Procedure of Vietnam 2015 provides:
"1. People's Courts of provinces shall have the jurisdiction to settle according to first-instance procedures the following disputes:
a) Civil, marriage- and family-related, business, trade or labor disputes prescribed in Articles 26, 28, 30 and 32 of this Code, except for disputes falling under the jurisdiction of the district-level people's Courts as provided for in Clause 1 and Clause 4 Article 35 of this Code;
b) Civil, marriage-and family-related, business, trade or labour petitions prescribed in Articles 27, 29, 31 and 33 of this Code, except for petitions falling under the jurisdiction of the district-level people's Courts as prescribed in Clause 2 and Clause 4 Article 35 of this Code;
c) Disputes and petitions prescribed in Clause 3, Article 35 of this Code."

Procedure 2004[124]. Hochiminh city is a central-affiliated city in light of Article 4 of Resolution 1211/2016/UBTVQH13 dated 25th May 2016 on Standards of Administrative Division and of Administrative Division Criteria and Article 1 of Resolution 27/2022/UBTVQH15. Hence, the Hochiminh People's Court has the jurisdiction to settle the allegation of Company A in Case Law 13/2017/AL[125].

According to Article 3 of Law on Organization of People's Court 2014, the Superior People's Courts is higher level than the People's Courts of Provinces or Centrally- affiliated Cities[126]. Hence, the appeal court, in this Case Law 13/2017/AL, would be the Hochiminh Superior People's Courts[127]. The Vietnam Supreme People's Court shall supervise the adjudicating work of the courts in this case law[128].

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[124] Article 35.2.dd of the Code of Civil Procedure 2004 provides:
"Territorial jurisdiction of courts
2. Territorial jurisdiction of courts to settle civil matters shall be determined as follows:
dd. The courts of the areas where the request senders reside or work, if they are individuals, or where the request senders are headquartered, if they are agencies or organizations, shall have the jurisdiction to settle requests not to recognize foreign courts' civil, marriage and family, business, trade or labour judgments or decisions, which are not required to be enforced in Vietnam."

Article 35.2.dd of the Code of Civil Procedure 2004 is now replaced by Article 39.2.dd of the Code of Civil Procedure of Vietnam 2015. Article 39.2.dd of the Code of Civil Procedure of Vietnam 2015 provides:
"Territorial jurisdiction of courts
2. Territorial jurisdiction of Courts to settle civil matters shall be determined as follows:
dd) The Courts of the areas where the petition senders reside or work, applicable to individuals, or where the petition senders are headquartered, applicable to agencies or organizations, shall have the jurisdiction to settle petitions for non-recognition of foreign courts' civil, marriage and family, business, trade or labour judgments or decisions, which are not requested to be enforced in Vietnam."

[125] The standards for central-affiliated cities are regulated in Resolution 1211/2016/UBTVQH13 and Resolution 27/2022/UBTVQH15 (effective from January 1, 2023) include:
(1) Population scale of central-affiliated cities
Central-affiliated cities have a population of 1,500,000 or more.
From January 1, 2023, the population scale must be 1,000,000 people or more.
According to the Vietnam General Statistics Office, the population scale of the 5 central-affiliated cities in 2021 are Ho Chi Minh City 9,166.84 thousand people; Can Tho city 1,246.99 thousand people; Da Nang city 1,195.49 thousand people; Hai Phong city 2,072.39 thousand people; Hanoi city 8,330.83 thousand people. See more at: https://www.gso.gov.vn/en/px-web/?pxid=E0201&theme=Population%20and%20Employment.
(2) Natural area of central-affiliated cities
Central-affiliated cities have a natural area of 1,500 km2 or more.
According to the General Statistics Office, the natural area of the 5 central-affiliated cities is Hanoi city 3,359.82 km2; Hai Phong city 1,526.52 km2; Da Nang city 1,284.73 km2; Ho Chi Minh City 2,095.39 km2; Can Tho city 1,440.40 km2. See more at: https://www.gso.gov.vn/en/population/.
(3) Administrative units affiliated with central-affiliated cities
Central-affiliated cities have at least 11 administrative units at the district level affiliated with them.

[126] Article 3 of Law on Organization of People's Court 2014 provides:
"Organization of people's courts
1. The Supreme People's Court.
2. Superior People's Courts.
3. Courts of provinces and central-affiliated cities.
4. Courts of rural districts, urban districts, towns, provincial cities and the equivalent.
5. Military courts."

[127] According to Article 1 of Resolution 957/NQ-UBTVQH13 dated 28th May 2015 on The Establishment Superior People's Courts, there are three Superior People's Courts in Vietnam which are Superior People's Court in Hanoi city, Superior People's Court in Hochiminh city and Superior People's Court in Danang city.

[128] Article 20 of Law on Organization of People's Court 2014 provides:
"Duties and powers of the Supreme People's Court

8.3.2. Analysis of Case Law

The Facts:

The plaintiff, Company A had entered an international contract (Contract No. FARCOM/RCN/IVC/036/2011, hereinafter referred to as "Sales contract") with the defendant, Company B on June 7, 2011.[129] Company B sold Ivory Coast raw cashew nuts to the plaintiff and received their payment by a deferred 90-day letter of credit starting from the date of delivery in the bill of lading (hereinafter referred to as "BL"). The BL contained the return condition which allowed the plaintiff to refuse the goods if the goods were below 45lbs/80kg or the count of nuts was 220 nuts/kg, or the maximum moisture was over 12%. Both parties agreed to choose Bank E as the issuing bank. Bank N- Singapore branch (hereinafter referred to as "Bank N") was picked by Company B as the confirming bank.

Vinacontrol was chosen to inspect the goods under the requirements of the Sales contract. Vinacontrol would inspect the goods by the time it was delivered to Ho Chi Minh city at the destination port. A deferred credit No. 1801ILUEIB110002 was issued for the payment of the Sales contract by Bank E- Branch D under the requirement of the plaintiff. The letter of credit No. 1801ILUEIB110002 (hereinafter referred to as "LC") was a part of the process of purchasing the goods.

Under the requirements of the plaintiff, Bank E issued the LC on 7 July 2011 which was governed by the UCP 600 and has essential requirements such as payment due dates or amount of payment. In this LC, the measure of security must be conducted by a *third-party guarantee*. The *identity* of the third-party inspector was not mentioned in the LC.

Afterwards, Bank N requested Bank E to reimburse under the letter of credit with 03 sets of documents with the details of payment requests on 25 and 29 July and 9 August 2011. Bank E then sent documents to the plaintiff to get confirmation from the plaintiff stating that they had received the full set of documents and promised to settle on time, at the same time, Bank E sent a notification relating to its acceptance of paying on predefined due dates.

The plaintiff confirmed that they had received the letter of credit with full value and on-time payment. With the confirmation of the plaintiff, Bank E - Branch D endorsed the draft.

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1. The Supreme People's Court is the highest judicial body of the Socialist Republic of Vietnam.
The Supreme People's Court shall review according to cassation or reopening procedure in accordance with the procedural law judgments and decisions of courts which have taken legal effect and are protested against.
2. To supervise the adjudicating work of other courts, except cases prescribed by a law.
3. To make overall assessment of adjudicating practices of courts, ensuring the uniform application of law in trial.
4. To train and retrain judges, assessors and other staffs of people's courts.
5. To manage people's courts and military courts organizationally in accordance with this Law and relevant laws, ensuring independence of courts from one another.
6. To submit to the National Assembly draft laws and resolutions; to submit to the National Assembly Standing Committee draft ordinances and resolutions in accordance with law."

[129] The identity of the plaintiff, defendant and third parties are kept secret in the original case law.

Company B then was negotiated without recourse by Bank N under the aforesaid 03 sets of documents. Under the guidance of UCP 600, Bank E honoured the complied documents presented by the confirming bank.

The plaintiff then had Vinacontrol examine the goods when they were delivered at the port of discharge according to Article 8 of the Sales contract. Due to the supervision, the plaintiff found out that the condition of the nuts was not satisfied the Sales contract requirements. The certificates of Vinacontrol had shown that the average outturn of the nuts was 37.615 lbs/80kg, which was lower than the refusal conditions described in the Sales contract. The plaintiff considered this as *commercial fraud*, hence, they tried to reach the defendant to solve the bad situation relating to the quality of the goods, but the defendant did not respond.

On 15 September 2011, the plaintiff brought the case to the Ho Chi Minh City People's Court with a Statement of Claims asking for an injunctive relief to stop Bank E's payment and requested the court to force the defendant to receive the shipment of goods back. Afterwards, on 12 August 2013, the plaintiff added another claim to the court asking for cancelling the underlying contract and the LC. Through the proper procedures, the defendant was summoned through the Ministry of Justice of Vietnam but was still absent at the hearing. On 23 September 2011, the First-instance Court then favoured the applicant with an injunctive relief named Decision on the application of the provisional measure No. 101/2011/QD-BPKCTT to postpone the payment of the letter of credit.

At the hearing, the plaintiff then asked the First-instance Court to cancel the Sales contracts as well as cancel the payment obligation of Company A under LC. At the same time, the plaintiff also wants the Court to compel Company B to receive the returned goods and required the Court to maintain the temporary injunction until the judgement became effective.

Bank E then disagreed with the request to cancel the letter of credit of the plaintiff and in its appeal, Bank E wanted the court to set aside the aforesaid Decision to let Bank E reimburse Bank N under the light of UCP 600 and international banking practice.

The fraud:

The plaintiff had Vinacontrol investigate the delivered nuts as agreed in the Sales contract. The quality of the nuts was determined they did not meet the standards required for quality specifications. Due to Vinacontrol's certificates regarding inspecting the quality and quantity of the nuts as well as their status, the results implicated that the average outcome of the cashew nut was 37.615lbs/80kg. This scale was extremely low compared to the declined requirement. The Buyer had considered this situation regarding the quality of the delivered nuts as commercial fraud; hence, they had attempted to contact the Seller several times to solve such a problem. However, the Seller did not respond.

Therefore, the Buyer brought the case to the Ho Chi Minh City's People's Court with a Statement of Claims on 15 September 2011. In the Statement, the Buyer claimed that there was

commercial fraud in the transaction since the outturn of the nuts was extremely lower than the refusal conditions as required in the Sales contract (the refusal condition is 45lbs). Hence, the Buyer requested the court to force the Seller to receive the shipment of the cashew nuts that the Buyer wanted to return. Furthermore, the Buyer did not agree to settle the contracted price and demanded the Court to issue a temporary injunctive relief requiring Bank E to pause the reimbursement to the Seller under the LC. This injunction must be continued until there were different rules from the Court.

The issue

The applicant and the banks stipulated in the sales contract that the UCP 600, the most recent UCP, would apply to their letter of credit. Therefore, the first question raised in this circumstance is whether Vietnamese legislation allows the UCP 600 to be used as a source of law for this transaction and the second question is whether the UCP could solve the "fraud" relating to the quality of the goods arising from the underlying contract.

For the first question, the UCP, which is a set of international commercial practices, is mentioned in the Law on Negotiable Instrument 2005. According to Article 6 of the Law on Negotiable Instrument, "In the case of negotiable instrument relationships involving foreign elements, the parties to the negotiable instrument relationship may agree to apply international commercial practices, including the International Chamber of Commerce's Rules on uniform practice for documentary credits and the Uniform Rules on the collection, and other relevant international commercial practices by regulations of the Government." (The National Assembly, 2005)[130]; as a result, the UCP could be chosen to govern the letter of credit involving foreign elements in Vietnam if the parties agree. However, the UCP 600 does not have fraud provisions as a result, Vietnam law must be used to address the fraud issue.

To solve the "fraud" problem, there are other questions raised which are whether the goods which did not achieve the quality inspections could be considered *fraud* by the seller under the letter of credit process in Vietnam legislation; and then once the delivery of nonconforming products is defined as *fraud* in the letter of credit, could the courts issue injunctive relief to protect the Vietnamese buyer from an oversea unscrupulous seller?

Contrary to the P.R.C. which has its fraud rules defined in the 2005 Rules or Section 5-109 of UCC in the US, Vietnam legislation has neither rules pertaining to the definition of fraud in the credit nor letter of credit law. Except for some specific commercial frauds which are defined in the Commerce Law of Vietnam 2005, most of the definitions of fraud shall be referred to regulations in the Civil Code of Vietnam. The general definition of fraud is defined in Article 132 of the Civil Code 2005 which is "an intentional act of a party or a third person for the purpose of misleading the other party as to the subject, the nature of the entity or the contents of the civil transaction which has caused the other party to enter into such transaction" (The

[130] The English translation of the Law on Negotiable Instrument of Vietnam is borrowed from the translation of the website thuvienphapluat.vn. See the original version at: https://thuvienphapluat.vn/van-ban/Tien-te-Ngan-hang/Luat-Cac-cong-cu-chuyen-nhuong-2005-49-2005-QH11-7023.aspx.

National Assembly, 2005)[131]. Even though this Article 132 explains fraud in civil transactions, this definition of fraud still can be considered in some legal context.

Since there are currently no regulations regarding the letter of credit law in Vietnam legislation, the ruling of the courts, in this case, shall be taken from the Vietnam Commercial Law and the Vietnam Civil Procedure Code. To be specific, the legal validity of Vinacontrol's certification shall be evaluated under Article 262.1 of Vietnam Commercial Law 2005 (The National Assembly, 2005)[132] and it shall be used as a piece of evidence in light of Article 83.5 of Vietnam Civil Procedure Code 2004 (The National Assembly, 2004)[133]. In case Vinacontrol's certification is considered appropriate proving the goods do not match the requirements, the seller shall be considered committing a fundamental breach; hence, the Sales contract could be cancelled due to Article 312.4.b[134] and Article 314.1[135] of Vietnam Commercial Law 2005 as an injunctive relief of the court (The National Assembly, 2005).

A. Findings of the Courts

The First-instance Court

The underlying contract was declared by the First-instance Court that it conformed to the regulations of the Commercial Law 2005 relating to the rights and responsibilities of the parties. As stated in Vinacontrol's certificates, the products did not meet the specifications of

[131] By the time this judgement is issued, the Vietnam People's Court used the Civil Code of Vietnam 2005. However, Article 132 of the Civil Code of Vietnam 2005 is now replaced by Article 127 of the Civil Code of Vietnam 2015. The definition of fraud in Article 127 of the Civil Code of Vietnam 2015 remains the same as Article 132 of the Civil Code of Vietnam 2005.

[132] Article 262.1 of the Commercial Law of Vietnam 2005 provides "Where contracting parties agree on the use of an assessment certificate issued by a particular trader providing assessment services, such assessment certificate shall be legally binding on all the parties if they cannot prove that the assessment results are non-objective, untruthful, or obtained with technical or professional errors."

[133] The English translation of the Civil Procedure Code of Vietnam 2004 is borrowed from the translation of the website thuvienphapluat.vn. See the original version at: https://thuvienphapluat.vn/van-ban/Thu-tuc-To-tung/Bo-luat-To-tung-dan-su-2004-24-2004-QH11-52189.aspx. By the time this judgement is issued, the Vietnam People's Court used the Civil Procedure Code of Vietnam 2004. Article 83.5 of the Civil Procedure Code of Vietnam 2004 provides "Expert conclusions shall be regarded as evidence if the expertise is conducted in accordance with the procedures prescribed by law." The Civil Procedure Code of Vietnam 2004 is expired and was replaced by the Civil Procedure Code of Vietnam 2015, which is valid in 2016 except for some provisions. Article 83.5 of the Civil Procedure Code of Vietnam 2004 is replaced by Article 95.6 of the Civil Procedure Code of Vietnam 2015. The language in Article 95.6 of the Civil Procedure Code of Vietnam 2015 remains the same as Article 83.5 of the Civil Procedure Code of Vietnam 2004.

[134] Article 312.4 of the Commercial Law of Vietnam 2005 provides "Except for cases of liability exemption specified in Article 294 of this Law, the remedy of cancellation of contracts shall be applied in the following cases:
a/ Upon commission of a breaching act which serves as a condition for the cancellation of the contract as agreed upon by the parties;
b/ Upon a substantial breach of contractual obligations by a party."

[135] Article 314.1 of the Commercial Law of Vietnam 2005 provides "Except for cases specified in Article 313 of this Law, following the cancellation of a contract, such contract shall be invalid from the time it is entered into, and the parties shall not have to continue performing their contractual obligations, except for their agreements on their post-cancellation rights and obligations and resolution of disputes."

the Sales contract, hence, the court considered that the defendant was at fault since he sent the non-conforming goods.

The legal validity of Vinacontrol's certification was valid under Article 262.1 of Vietnam Commercial Law 2005 (The National Assembly, 2005) and it shall be used as evidence in light of Article 83.5 of Vietnam Civil Procedure Code 2004 (The National Assembly, 2004). Hence, according to Vinacontrol's certification, the products did not meet the specifications *in the underlying contract*, so the seller was considered committing a fundamental breach based on Article 3.13 of Vietnam Commercial Law 2005[136] because the applicant could not reach its original goal which made them join the contract. The Sales contract was cancelled due to Article 312.4.b and Article 314.1 of Vietnam Commercial Law 2005 (The National Assembly, 2005). Under Article 39 of the Vietnam Commercial Law 2005[137], the plaintiff had the right to refuse the goods (The National Assembly, 2005).

Hence, the First-instance Court cancelled the contract under Article 3.13 and Article 312 of the Vietnam Commercial Law (The National Assembly, 2005). The First-instance Court considered the LC as an integral part of the Sales contract; hence, the LC was cancelled because the underlying contract was invalid. Hence, the reimbursement obligation in the letter of credit of Bank E to Bank N was cancelled because the LC was cancelled. Furthermore, the Buyer could receive their deposit from Bank E. The temporary injunction should be continued to apply until the decision of the First-instance Court was valid.

The fraud tests

Company A bring the case to the court claiming there was *commercial fraud* based on the disqualification of the nuts. The First-instance Court's ruling affirmed that there had been *commercial fraud* and that the duplicitous Seller should not have been protected by the UCP 600. As was previously mentioned, the independent principle prevented the banks' payment obligations from being suspended throughout the letter of credit procedure. Due to the autonomous concept of the letter of credit, the bank's only obligation is to make payments against the completed paperwork. The fraud rules are the lone exception to the independent

[136] Article 3.13 of the Vietnam Commercial Code 2005 provides "Substantial breach means a contractual breach by a party, which causes damage to the other party to an extent that the other party cannot achieve the purpose of the entry into the contract."

[137] Article 39 of the Vietnam Commercial Law 2005 provides: "Goods which are not appropriate to contracts
1. Where it is not specified in the contract, goods shall be considered not appropriate to the contract when they fall into one of the following cases:
a/ They are not suitable for common use purposes of goods of the same type;
b/ They are not suitable to any specific purpose that has been notified by the purchaser to the seller or the seller should have known at the time the contract is entered into;
c/ Their quality is not the same as the quality of the samples previously handed over by the seller to the purchaser;
d/ They are not preserved or packaged by a method common to such goods, or not preserved by proper preserving methods in cases where no common preserving method is available.
2. The purchaser may reject the goods if such goods are not appropriate to the contract according to the provisions of Clause 1 of this Article."

principle. In Case Law No. 13/2017/AL, at first, the First-instance Court had admitted the function of the letters of credit as well as the application of the UCP 600 as follows[138]:

> "The letter of credit is an absolute undertaking of the issuing bank to provide the payment for the beneficiary if he presents the documents complying with the requirements in the letter of credit. The essence of the letters of credit is the payment to the Seller which will be certainly conducted if the Seller presents the conforming documents. The presented documents must be evaluated either complied or not and the Beneficiary must be responsible for the accuracy of the documents. […] The UCP 600 is issued to make the international payments run smoothly, once parties choose to apply UCP 600, they must respect and are not allowed to arbitrarily violate the rules."

The First-instance Court ruled that there had been commercial fraud and ordered the banks to abide by its ruling as follows:

> "However, as has been analysed, after the dispute happened, the Buyer brought the case to the People's Court requesting adjudicating. The Trial Panel has sufficient grounds to define that the documents presented by the beneficiary are invalid because the goods do not achieve the required quality, the Buyer is not obligated to pay for the goods, hence, *parties must comply with the judgement of the Court and cannot invoke the UCP to force the Buyer to pay for the Seller when* ***the Seller has committed commercial fraud***."

And the First-instance Court looked beyond the presented documents and seriously considered the facts that happened under the Sales contract:

> "As long as the requirements under the letter of credit are fulfilled and the Beneficiary tenders the conforming documents, the payment is guaranteed. If the documents do not comply with reality (non-conforming documents), the bank must refuse to pay."

As has been seen, the First-instance Court expressed that the provisions of the UCP should be retained; however, such provisions should not be invoked to protect the seller once the seller committed fraud. The First-instance Court had looked beyond the presented documents and required the banks to refuse to pay if there were discrepancies between the documents and the reality. The judgement of the First-instance Court had set a new perspective on the application of the UCP in Vietnam. Even though the First-instance Court did not refer to any other fraud rules or had guidance from Vietnam legislation regarding the fraud in the letter of credit law, the opinions of the First-instance Court regarding the fraud in the letters of credit were still proper and expressed the main idea that the independent principle should not be used to protect the fraudulent activities. According to the court, banks should prohibit payments under letters of credit in cases of fraud and shouldn't invoke the independent principle to defend dishonest

[138] The English translation of the First-instance Court's judgement is translated from the original version by the author. See the original version at: https://anle.toaan.gov.vn/webcenter/portal/anle/anle.

sellers. Hence, the First-instance Court had considered commercial fraud in this instant case as fraud in letters of credit and favoured the applicant with an injunctive relief to postpone the payment of the letter of credit. This means the First-instance Court believes that once fraud happens in the letter of credit, suspension of payment should be issued to safeguard the innocent parties.

Since the disqualification nuts did not fit either the fraud criteria in Article 132 of the Vietnam Civil Code 2005 or the fraud standards in the 2005 Rules or the "material fraud" in Section 5-109 of UCC, the key issue, in this case, was whether the disqualification nuts were, as the Buyer alleged, fraud in the letter of credit. Injunctions to delay the payment may be utilised if the disqualification nuts are fraud in the letter of credit. Additionally, the claim made by the First-instance Court that the LC was cancelled because it constituted a crucial component of the illegal contract was untrue.

The Appeal Court

Bank E then submitted to the Court of Appeal an appeal for the entire aforesaid judgement of the First-instance court. A decision was issued to open a hearing and summoned the parties to be presented in the hearing on 25 September, 27 October, and 31 October 2014; the last date was 16 April 2015. However, these hearings were put off because of several reasons. Another Decision on May 29, 2015, was issued by the Court of Appellate to halt the hearing to continue the judicial entrustment procedures to summon Company B.
However, the Decision on 29 May which is used to postpone the appellate hearing is considered not to comply with Article 13.2 of Resolution No. 06/2012/NQ-HDTP dated 03 December 2012 issued by the Judicial Council of the Supreme People's Court[139]:

> "In case there is a decision on temporary suspension of the appellate hearing of a civil case, the time limit for hearing preparation ends on the date of such decision on temporary suspension. The time limit for appellate hearing preparation re-commences from the date on which the appellate court continues the appellate hearing when the reason for such temporary suspension ceases".

Bank E was not present, making this hearing the first time the Court had properly summoned them. The request to postpone the hearing due to Mr K, Bank E's representative, taking a business vacation was later denied by the Appellate Court.

According to the Decision on suspension of the appellate hearing No. 29/2015/QDPT-KDTM dated 26 August 2015, the Superior People's Court in Ho Chi Minh City ruled:

[139] The English translation of Resolution No. 06/2012/NQ-HDTP is borrowed from the translation at the website thuvienphapluat.vn. See the original version at: https://thuvienphapluat.vn/van-ban/Thu-tuc-To-tung/Nghi-quyet-06-2012-NQ-HDTP-huong-dan-phan-thu-ba-Bo-Luat-to-tung-dan-su-sua-doi-193784.aspx.

- To suspend the appellate hearing over Commercial Case No. 29/2015/QDPT-KDTM dated 26 August 2015 (hereinafter referred to as "Commercial Case") on "Dispute on contract for the sale of goods".
- First-instance Commercial Judgment of the People's Court of Ho Chi Minh City takes effect on 26 August 2015.

Bank E then submitted a request to the Chief Justice of the Supreme People's Court for consideration of the aforementioned first-instance commercial judgment and Decision on suspension of the appellate hearing under the cassation procedures.

In Decision No. 11/2016/KN-KDTM dated 7 March 2016, the Chief Justice of the Supreme People's Court protested against the Decision on suspension of the appellate hearing over the Commercial Case by the Superior People's Court in Ho Chi Minh City; requested the Judicial Council of the Supreme People's Court to conduct the cassation procedures to set aside Decision on suspension of the appellate hearing No. 29/2015/QDPT-KDTM dated 26 August 2015 by the Superior People's Court in Ho Chi Minh City and First-instance Commercial Judgment No. 356/2014/KDTM-ST dated 7 April 2014 of the People's Court of Ho Chi Minh City; transfer the case file to the People's Court of Ho Chi Minh City re-conduct the first-instance procedures in accordance with the law.

At the cassation hearing, the representative of the Supreme People's Procuracy requested that the Judicial Council of the Supreme People's Court accept the protest of the Chief Justice of the Supreme People's Court.

B. The Vietnam Supreme People's Court decision

The Supreme People's Court considered that the ruling of the First-instance Court relating to the cancellation of the Sales Contract was reasonable under Article 3.13 and Article 312 of the Commercial Law 2005[140]. However, the cancellation of the Sales contract was not proper. According to the Supreme People's Court, the First-instance Court did not solve the compensating for the applicant for damages. These problems made the case was not correctly resolving.

[140] The English translation of the Opinions of the Vietnam Supreme People's Court are translated from the original version by the author. See the original version at: https://anle.toaan.gov.vn/webcenter/portal/anle/anle.

The Supreme Court then referred to Article 3.4 of the Law on Credit Institutions 2010[141], Article 16.1[142] and Article 19[143] of Decision No. 226/2002/QD-NHNN[144] for further regulation regarding the letter of credit. In the letter of credit, the parties agreed to have LC governed by the latest UCP, the UCP 600, and the Supreme People's Court respected this agreement. The Decision of the Appellate Court to suspend the hearing was set aside by the Supreme People's Court and the case was transferred back to the People's Court of Ho Chi Minh City.

a. The opinion of the Vietnam Supreme People's Court about the application of UCP 600

The Vietnam Supreme People's Court agreed that the LC was governed by the UCP 600 due to "the contents of the LC", then "the LC is governed by and applies the Uniform Customs and Practice for Documentary Credits, with the most recent version (currently UCP 600)." Under the guidance of the UCP 600, the Vietnam Supreme People's Court recognized the irrevocable feature of the letters of credit in Article 2 of UCP 600 and the independent principle in Article 4 (International Chamber of Commerce, 2007). The Supreme People's Court also considered the obligation to deal with the documents only of the banks in the letter of credit according to Article 5 of UCP 600 (International Chamber of Commerce, 2007). The obligation of the bank in Article 15(a) of UCP 600 was also recognized by the Supreme People's Court (International Chamber of Commerce, 2007). With all basics that were mentioned, the Supreme People's Court declared that the LC was a separate undertaking with the Sales contract between Company A and Company B. The ground for this declaration was based on the independent principle under the guidance of Article 4 of the UCP 600 (International Chamber of Commerce, 2007). The Vietnam Supreme People's Court expressed that the reimbursement of Bank E also must be continued under the UCP 600, and the payment obligation of the banks in the letter of credit must be continued despite problems arising from the underlying contract.

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[141] Article 3.4 of the Law on Credit Institutions 2010 provides:
"Organizations and individuals engaged in banking operations are entitled to reach an agreement on the application of commercial practices, including:
a/ International commercial practices provided by the International Chamber of Commerce.
b/ Other commercial practices which are not contrary to the Vietnamese law.".

[142] Article 16.1 of Decision No. 226/2002/QD-NHNN provides:
"Letter of credit shall be a conditional written undertaking opened by banks at the request of a payment service user (the applicant for opening the letter of credit), under which, banks shall perform the requests of the payment service users (the applicant for opening letter of credit) in order to:
- Effect the payment or authorize other banks to effect the payment immediately at the instruction of the payee upon receipt of a set of presented documents satisfying the conditions of the letter of credit; or
- Accept to make the payment or authorize other banks to make the payment at the instruction of the payee at a specific future time upon receipt of a set of presented documents satisfying conditions of the letter of credit.".

[143] Article 19 of Decision No. 226/2002/QD-NHNN provides:
"1. Payment by letter of credit: The opening, issuance, amendment, notification, confirmation, examination of documents, payment and rights, obligations, etc. of related parties in payment by letter of credit shall be performed in accordance with general principles on documentary credits issued by the International Chamber of Commerce (ICC) and applicable upon agreement of parties engaging in the payment in accordance with current applicable Vietnamese laws.
2. Payment by international payment cheques, payment orders, payment authorizations, collection orders, collection authorizations, international cards, and other forms of payment: process, and procedures of payment shall be performed in accordance with international custom and rules and agreements provided that they are not contrary to Vietnamese laws.".

[144] Decision No. 26.2002/QD-NHNN expired in 2015.

As previously mentioned, if a letter of credit in Vietnam specified that it would be controlled by the UCP, the Supreme People's Court of Vietnam acknowledged such applicability. The independent principle of the letter of credit was also emphasised by the Vietnam Supreme People's Court, which said that this concept needed to be upheld. The Supreme People's Court of Vietnam also noted that all Vietnamese People's Courts must uphold the notion that a letter of credit's independence is crucial. Even though the Sales contract was void, banks were still required to make payments without interruption.

b. The fraud test of the Vietnam Supreme People's Court

The Supreme People's Court had accepted the independent principle in the letters of credit and expressed that the main core of the documentary credit was the documents. The documents are the main part of such transactions, not the products. Hence, the Vietnam Supreme People's Court believed that the banks must check the documents with modest care to assure that the documents conform to the criteria of the letter of credit. The Vietnam Supreme People's Court also stated that the banks should not bear the burden of the facts that happened beyond the submitted documents as the First-instance Court had stated.

The Supreme People's Court noticed the inspection certifications along with the set of documents issued by an independent assessor. The LC *did not* contain any requirements relating to the goods being inspected at the port of destination by a specified inspector. Such lacking provision makes the requirements in the LC different from the requirements in the Sales contract. The inspected certificate issued by a foreign inspector had complied with the conditions under the LC; hence, under the independent principle, the Seller could submit the documents with aforesaid certificates to the bank and required the payment in full and on time. Hence, the Supreme People's Court considered that the First-instance Court had issued their ruling based on the inspection certificates of Vinacontrol at the port of destination was contrary to the requirements under the credit LC and Company B's commitments, and such ruling *was not appropriate* according to the practice of the UCP.

The Supreme People's Court had determined that Bank E was required to reimburse Bank N after Bank N had honoured the papers submitted by the Seller under the letter of credit. The Supreme People's Court believed that the First-instance Court's ruling that the LC was an integral part of the underlying contract and that it lost its validity when the contract was terminated was incorrect. This ruling went against UCP 600 rules and lacked sufficient supporting evidence.

C. Analysis of the Case Law

a. The application of the UCP in Vietnam

In Case Law No. 13/2017/AL, one of the main questions is whether the UCP 600 could be able to apply to govern the international letters of credit in Vietnam. The UCP provisions are not

law, and the ICC also has no authority to legislate. The UCP is a set of rules that describe the banking practice and may reflect trade usage. Regarding the role of practice for international commercial practice, Article 5 of the Vietnam Commercial Law 2005 provides that parties are allowed to apply international commercial practice if such practice "is not contrary to the fundamental principles of the Vietnamese law" (The National Assembly, 2005).

Furthermore, according to the Law on Negotiable Instrument 2005, Article 6 has stated as follows:

> "Negotiable instrument relationships involving foreign elements, the parties to the negotiable instrument relationship may agree to apply international commercial practice"

The "international commercial practice" under Article 6 includes the Uniform Customs and Practice for Documentary Credits. In other words, the UCP could be applied in the letters of credit in Vietnam if the parties agree. Hence, UCP 600 can govern the LC in Case Law No. 13/2017/AL as the parties agreed.

The First-instance Court also agree with the regulations of UCP 600 to govern the LC as follows:

> "The UCP 600 is issued to make international payments run smoothly, once parties choose to apply UCP 600, they must respect and are not allowed to arbitrarily violate the rules."

In this instant case, the Vietnamese Supreme People's Court also applied the UCP as a source of international banking practice and UCP could be used to govern the LC. Furthermore, the Supreme People's Court had adopted the thinking and interpretation of the UCP 600 about the independent principle into their consideration. Even though UCP 600 is not law, it contains useful provisions from which to explain the intention of parties. In the absence of any laws governing letter of credit transactions and any other authoritative interpretations that might apply to the case in Vietnam, UCP 600 is a subsidiary source of regulation regarding the international banking practice that a court should consider as a reasonable basis for its judgement in the letter of credit law.

b. The fraud exception

Since there is no fraud provision in the UCP 600, the ICC believes that this matter should continue to be dealt with within local law. Therefore, Vietnam law must be consulted on the fraud problem raised by Company A in Case Law No. 13/2017/AL. However, there is presently no letter of credit law in Vietnam, nor are there any particular prohibitions for fraud in the letter of credit transactions. Therefore, the Vietnam Commercial Law and Vietnam Civil Code will serve as the primary sources for the definition of fraud. The author also intends to make reference to the 2005 Rules of PRC while assessing the laws governing fraud in the Vietnamese

judicial system for Case Law No. 13/2017/AL. Given the similarities between the two nations, it will be appropriate to analyse the fraudulent activities by consulting the 2005 Rules. The author also wants to compare the fraud standards in Case Law No. 13/2017/AL to Section 5-109 of UCC.

The general concept of "fraud" (lừa dối) in the Vietnamese legal system is illustrated in Article 132 of the Vietnam Civil Code 2005 as "an intentional act of a party or a third person for the purpose of misleading the other party as to the subject, the nature of the entity or the contents of the civil transaction which has caused the other party to enter into such transaction." (The National Assembly, 2005)[145]. Fraud in the civil transaction is established when there is an intention from a party which make the other party misleading about the "subject, the nature of the entity or the contents". Since Vietnam legislation has neither rules relating to the definition of fraud in the letter of credit nor letter of credit law, this definition can be used for evaluating fraudulent activity in Case Law No. 13/2017/AL. This concept of fraud is considered an essential tool in defining fraud in this instant case.

In Section 5-109 of the UCC dealing with fraudulent activities, the standard of fraud is "material" (Uniform of Commercial Code, 1995). However, Article 5 does not give any further instruction relating to the definition of "material". Hence, the courts must deal with the definition and explain it from their perspective. Once there are any allegations regarding "material" fraud, the courts must examine the documents and the underlying transaction. According to Comment 1 in Section 5-109 of the UCC, examining the underlying transaction is the only way to figure out whether the beneficiary committed fraud, or the document is forged, and "if so, whether the fraud was material" (Uniform of Commercial Code, 1995).

Regarding the 2005 Rules, the fraud standards are made with a very narrow approach. Only no documents and the beneficiary fabricate them, or if the information contained in the documents given to the bank is false, the documents would be deemed fraudulent. Or only situations in which there are no products at all or only things with zero value are eligible to use the fraud rules. Another way to put it is that parties cannot invoke the fraud exception clause if items are delivered in poor condition or with missing units since it will not be considered fraud.

According to what has already been said, the First-instance Court held the view that the independent principle should not be applied to shield the dishonest seller and that banks should

[145] Article 127 of the Vietnam Civil Code 2015 has replaced Article 132 of the Vietnam Civil Code 2005. Article 127 provides: "Invalidity of civil transactions due to deception, threat or compulsion
Any party entering into a civil transaction as a result of deception, threat or compulsion has the right to request a court to declare such transaction invalid.
Deception in a civil transaction means an intentional act of a party or a third person for the purpose of misleading the other party as to the subject, the nature of the entity or the contents of the civil transaction which has caused the other party to enter into such transaction.
Threat or compulsion in a civil transaction means an intentional act of a party or a third person which compels the other party to conduct the civil transaction to avoid danger to the life, health, honour, reputation, dignity and/or property or that of its relatives."

discontinue fulfilling their payment obligations in the event of fraud. However, concerning the disqualification of the goods in the case law, if we apply the definition of fraud in Article 132 of the Vietnam Civil Code 2005 to this issue, the disqualification of the nuts is not enough to be considered fraud in the letter of credit. The intention of Company B which was sending the disqualification nuts is not enough to consider it has the "purpose of misleading the other party" (The National Assembly, 2005).

If the fraud standards of the 2005 Rules are consulted in Case Law No. 13/2017/AL, the fundamental breach in Case Law No. 13/2017/AL is also not fraud in the letters of credit. If the "material fraud" of Article 5 of the UCC is applied in Case Law No. 13/2017/AL, the fundamental breach in Case Law No. 13/2017/AL is also not "material fraud" in the letters of credit. There are some rules from some cases of law to define what actions could be considered material fraud (Itek Corp. v. First Nat. Bank of Boston, 1983) (Intraworld Industries v. Girard Trust Bank, 1975) (Roman Ceramics Corp. v. Peoples Nat. Bank, 1983) (Itek Corp. v. First Nat. Bank of Boston, 1983)[146] including the honour has no actual foundation (Dynamics Corp. v. Citizens & Southern National Bank, 1973)[147], the whole transaction is damaged by the fraudulent activities of the beneficiary (Intraworld Industries v. Girard Trust Bank, 1975)[148] and the underlying contract clearly expresses that the beneficiary is not allowed to draw on in that specific situation (Itek Corp. v. First Nat. Bank of Boston, 1983)[149]. Considering the products were sent in quality and quantity matched with the LC, the disqualification of the goods is not fraud and hence, the commercial fraud that the Buyer claimed in Case Law No. 13/2017/AL could not be used to invoke any injunctions.

As can be observed, the First-instance Court had made a very clear notification that the independent principle should not be used to shield the dishonest parties in the letter of credit and that the banks should not use this principle to nag with the court even though it is recorded in UCP 600 and is the main core of the uniquely of letters of credit. This point of view is a fresh orientation of the court, however, the foundation for this judgement based on commercial fraud is not well-established and lacks fraud standards. Nonetheless, the orientation of the First-instance Court pointed out that once fraud is included in letters of credit, injunctive relief should be invoked to protect the interest of innocent parties.

Contrary to the First-instance Court's opinions, the Vietnam Supreme People's Court clearly expressed its statements that the independent principle should be strictly followed to protect

[146] In the case *Itek Corp. v. First Nat'l Bank of Boston*, the holding stated that the injunctive relief would be deceived by the court to prevent the issuer to honor the documents while the beneficiary "did not even have a colorable claim".
[147] In the case *Dynamics Corp. of Am. v. Citizens & S. Nat'l Bank*, the court noted that the beneficiary could not take advantages on the situations and took the plaintiff's money without basic in fact.
[148] In the case *Intraworld*, the court noted that the injunctive relief could only be issued in case the entire transaction was vitiated which made the original obligation of the issuer- which was the independent principle- become disappear.
[149] In the case *Itek Corp. v. First Nat'l Bank of Boston*, the fraud exception "recognizes the unfairness of allowing a beneficiary to call a letter of credit under circumstances where the underlying contract plainly shows that he is not to do so."

the unique process of the letter of credit. The Supreme People's Court had emphasized that the transactions of the letters of credit are performed with documents, not products, and the banks were only required to examine the compliance of the documents with reasonable care. The bank should not be concerned about the items that did not adhere to the terms of the sales contract. The Vietnam Supreme People's Court precisely illustrated that the independent principle must be followed and strictly performed. However, the fraud rule was not mentioned in the opinion of the Supreme People's Court. The orientation of the Vietnamese Supreme People's Court is pertinent to the circumstances and the UCP's provisions; but it is clear that since there are no fraud standards for letter of credit law, this might lead to more issues and jeopardise the stability of Vietnam's financial sector. With fraud rules, in case a forgery is established, and the bank is involved in the forgery, or the banks know about such behaviour, the bank can exclude the independent principle and dishonour the letter of credit. Such a lack of provisions related to the fraud rules could harm the framework of letters of credit, the stability of the banking industry in Vietnam, and their reputations.

It was obvious to see that the Vietnamese Supreme People's Court wanted to keep the original payment procedure of letters of credit and did not want to meddle in such a process, even if there was fraud, in their opinion. Instead, the First-instance Court thinks that the independent principle should not be used to defend dishonest parties and that the fraud should be acknowledged in the letter of credit. The fraud standards are the main controversy in the First-instance Court's decision; without them, the court will struggle to distinguish between fraud that may be fraud in the letter of credit and fraud that is just ordinary commercial fraud. The perspectives of the First-instance Court and the Vietnamese Supreme People's Court in this case on fraud in letters of credit may serve as an illustration of the various court perspectives in Vietnam. Even though this case law cannot fully summarise the circumstances surrounding fraud in letters of credit in Vietnam or provide an overview of the Vietnamese courts' overall perspective on the fraud, it may be useful to provide a concise synopsis that is noteworthy of referencing. Having fraud rules in letter-of-credit legislation for Vietnam's legal system might lessen the frustration of Vietnamese judges who must define standards of fraud in the letters of credit by consulting other definitions of fraud in civil law or commercial law. Furthermore, judges will have a base to draw upon when dealing with a case involving fraud in letters of credit in the future, and it may also assist decrease violations of the letter of credit procedure. There is a chance that the judges will violate the letter-of-credit transaction process, which will have a serious impact on the stability of letters of credit as well as the Vietnamese banking system.

CHAPTER IX

THE FRAUD RULES RECOMMENDATION FOR VIETNAM

9.1. The Current Situation in the Economy of Vietnam

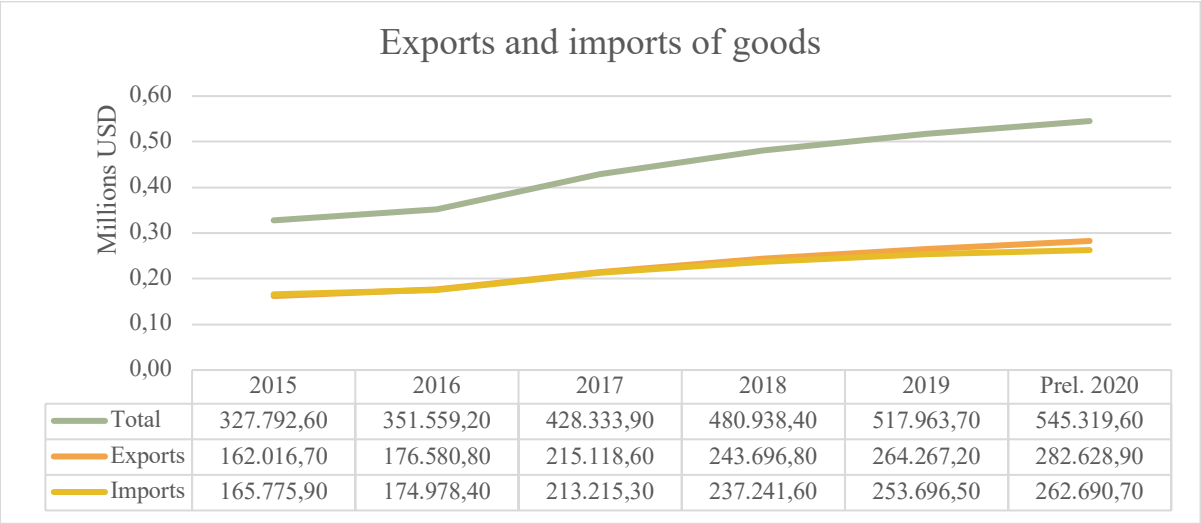
For international letters of credit, the banks will look for the international practice in the UCP for answers, as well as the definitions and processes. The applicants in letters of credit are expected to bear the risks which are fraud or forged documents. Bankers also expect that in case of fraud, the courts would issue their judgments based on international standard practice. Hence, it is extremely important for Vietnamese People's Courts to recognize the letter of credit as a special financial mechanism. However, Case Law No. 13/2017/AL has shown that the courts need a specific regulation to issue injunctive relief while retaining the commercial utility of letters of credit. Case Law No. 13/2017/AL is an illustration of the lack of fraud rules in letters of credit in Vietnam. Since the law of letters of credit is a complex area, the courts must be very careful in issuing their judgments. The Vietnamese legal system will be under pressure from international letters of credit experts if the courts keep interfering with the payment obligations of the banks as well as the positions of Vietnamese banks in international trading will be endangered. The courts in issuing their judgments must recognize the international practice of letters of credit, not "what is reasonable, fair, or equitable?" (Barnes, 1996).

The recommendations the author suggests are that the fraud rules should be drafted by reference to the contractual relation of the applicant and the issuer and comply as strictly as possible with the practice and usages of the UCP. At the same time, consulting with other fraud rules should be seriously considered.

As a civil law country, issuing fraud rules will impose a huge effect on the Vietnamese legal system because the people's courts trust and refer to the statutes and codes than the case law. However, the Vietnamese legal system barely mentions the law of letter of credit and fraud rules. There are a few regulations mentioned about letters of credit such as the Law on Negotiable Instruments 2005 "[t]he parties to the negotiable instrument relationship may agree to apply international commercial practices, including the International Chamber of Commerce's Rules on uniform practice for documentary credits and the Uniform Rules on collection …". However, the fraud rules for letters of credit do not exist in the system.

The lack of regulations relating to fraud rules is noticeable and must be adjusted since Vietnam is considered a good destination for international merchants. The information herein presented is borrowed from the General Statistic Office of Vietnam[150], which show the development in the export and import activities from the period 2015-2020. Among these activities, several transactions use letters of credit as payment methods.

[150] See more at: https://www.gso.gov.vn/en/homepage/



	2015	2016	2017	2018	2019	Prel. 2020
Total	327.792,60	351.559,20	428.333,90	480.938,40	517.963,70	545.319,60
Exports	162.016,70	176.580,80	215.118,60	243.696,80	264.267,20	282.628,90
Imports	165.775,90	174.978,40	213.215,30	237.241,60	253.696,50	262.690,70

Figure 1- Import and export of Goods

Source: General Statistic Office of Vietnam

In general, the Vietnam economy is growing up in recent years. From the period 2015 to 2020, the total exports and imports have grown 217 526,4 million US dollars more, which is quite impressive. In 2020, the exports are slightly higher than the imports (19 938,2 million US dollars). The higher development of the economy, the bigger demand for using financial services to set up settlements for international transactions. Besides the development of the economy, fraudulent activities have been proven to bloom and take advantage of payment services as well.

Under Article 4.15 of the Law on Credit Institutions 2010, letters of credit are a part of financial services including payment provisions using bank accounts in Vietnam (Vietnam National Assembly, 2010). There are millions of US dollars are spent each year in Vietnam on financial services. For example, in 2015, the number of imported financial services was only 219 million US dollars. While in 2020, the numbers are pre-calculated as 270 million USD. The chart below shows the statistics of the payment services in Vietnam from 2015-2020:

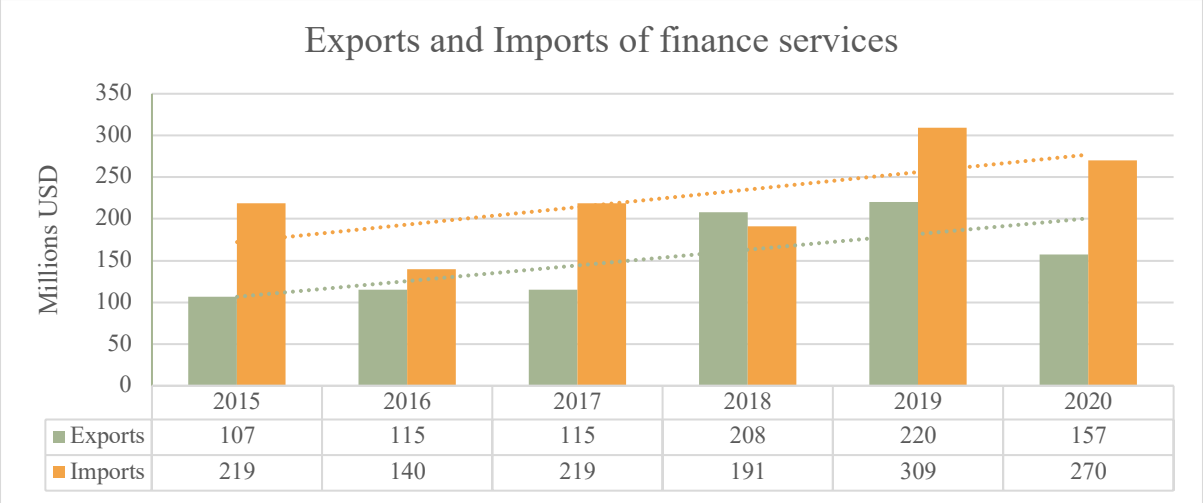


Figure 2: Exports and Imports of Financial services

Source: General Statistic Office of Vietnam

Based on the chart above, the exported and imported financial services of Vietnam are growing. To be specific, Vietnam mostly imports financial services. However, in 2018, the imports were higher than the exports by 17 million US dollars. The number of imported financial services in 2019 reached the highest point in the last five years (309 million US dollars). In recent years, the demands for using financial services in Vietnam are becoming larger and so does letters of credit.

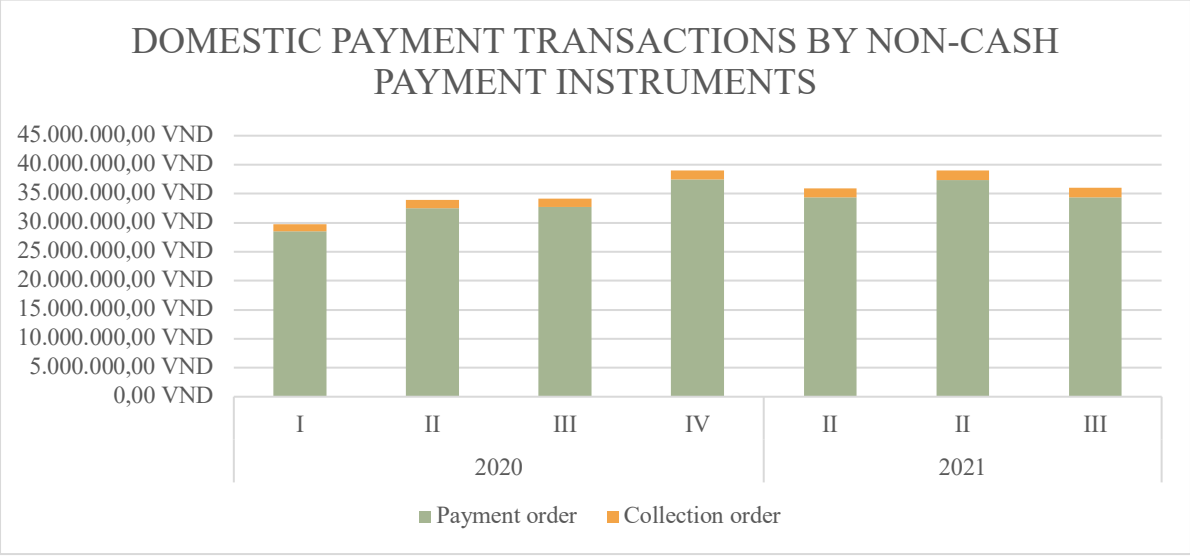


Figure 3: Domestic payment transactions by non-cash payment instruments

Source: The State Bank of Vietnam[151]

[151] See more at https://www.sbv.gov.vn/webcenter/portal/en/home/sbv/statistic/settleactiv/dtbmol?_afrLoop=24126199470123311#%40%3F_afrLoop%3D24126199470123311%26centerWidth%3D80%2525%26leftWidth%3D20%2525%26rightWidth%3D0%2525%26showFooter%3Dfalse%26showHeader%3Dfalse%26_adf.ctrl-state%3Dpet8rysm0_309.

In the light of Article 4.15 of Law on Credit Institutions 2010 and the chart above, among other payment transactions by non-cash payment instruments, the payment orders which include letters of credit made up 28.486.710,18 billion Vietnam Dong in the first quarter of 2020 and reached the highest number which was 37.324.174 billion Vietnam Dong in the fourth quarter in the same year. The value of the transactions remains stable during the last 2 years above 30.000.000 billion Vietnam Dong. Such numbers prove that the letter of credit is a favourite mechanism in Vietnam.

However, fraudulent activities in letters of credit are considered serious in recent years, especially when technology is developing. The numbers of fraudulent activities reported in by the International Maritime Bureau such as the 400 Million US dollars of metals trading and processing company in the United Arab Emirates (Solo Industries UK Ltd v. Canara Bank, 2001) or the loss of 200 Million US dollars of a single bank (ICC Commercial Crime Services, 2002, pp. 26-28). In Vietnam, the situation needs more recognition. In 2016, serious fraudulent situations in seafood exports were reported which made a few Vietnam companies lose hundreds of thousands of US dollars. The case started with Vietnam enterprises exporting seafood to a company called Echopack Inc, represented by Jason Brown (buyer), whose address at 5084 Francois, Cusson Lachine, Quebec, Canada (Vietnam Association of Seafood Exporters and Producers, 2016, p. 4). Exporters were paid via General Equity Bank (representing Echopack Company at Level 4, General Equity House, 17 Albert Street, Auckland 1010, New Zealand), via a 60-day letter of credit (hereinafter referred to as "LC") (Vietnam Association of Seafood Exporters and Producers, 2016, p. 4). LC was opened with two risky terms including the buyer would get a bill of lading to get the goods when the goods arrived and the signatures of the buyer at the issuing bank must coincide with the signatures of the buyer in the underlying contract signed with the seller (Vietnam Association of Seafood Exporters and Producers, 2016, p. 4).

After the shipment of Vietnamese seafood arrived at the port assigned by the buyer, Echopack took the goods (Vietnam Association of Seafood Exporters and Producers, 2016, p. 4). Later, the confirming banks in Vietnam sent the documents to General Equity Bank requesting to pay. However, the General Equity Bank delayed reimbursing the Vietnamese banks and refused to pay due to discrepancies in documents. Later, the General Equity Bank sent an email notifying that the signatures in the documents that the confirming bank submitted were different from the signatures of the applicant that the issuer had on the documents were presented by the applicant to register to open the letter of credit (Vietnam Association of Seafood Exporters and Producers, 2016, p. 4). Afterwards, they sent the documents back to Vietnam, however, these documents came back without one out of three original bills of lading. Even though the General Equity bank knew the documents were invalid, they still let Echopark get the original bill of lading to get the goods (Vietnam Association of Seafood Exporters and Producers, 2016, p. 4). Buyers and confirming banks could not conclude whether the signatures of the buyer within the documents matched the ones on the documents which are used to register to open LC because there were no signature models to compare (Vietnam Association of Seafood Exporters and Producers, 2016, p. 4). The whole process depended entirely on the General Equity Bank (Vietnam Association of Seafood Exporters and Producers, 2016, p. 4).

According to Vietnam Export and Processing Association, in 2015 - 2016, Vietnam lost 8 billion US mostly due to fraudulent activities (Nguyen Trong Thuy, 2019). Hence, fraud rules are highly needed in the current situation. The fraud rules, and the letter of credit law, in general, will uphold the courts when dealing with specified cases related to letters of credit and the frustrations of the courts will be solved when most of the provisions are combined in one set. Hence, the legal framework of Vietnam should have fraud rules and other regulations relating to letters of credit to keep up with the development in Vietnam.

9.2. The Suggestion for Vietnam

As indicated, the UCP 600 is widely accepted in Vietnam's legal rules, the banks in Vietnam also voluntarily subject themselves to the provisions of the UCP, hence, the new regulations must consult the UCP procedures for further explanation. However, the UCP 600 is not complete because of the shortage of fraud rules. The litigation might be raised relating to several problems such as the rights and obligations of the parties once the documents presented involve frauds or remedies. The courts must look for another appropriate body of law (Wood, 2008).

Despite the fact that Case Law No. 13/2017/AL did not specifically address the letter of credit fraud and cannot fully capture the circumstances surrounding the use of letters of credit in Vietnam, it is important to note that Vietnam’s legal system has a weakness with regard to the letter of credit fraud. Although the opinions of the Vietnam Supreme People's Court safeguard the reputation of Vietnamese banks, they could harm the sincere applicant in the event of fraud. The recommendations of the Vietnam Supreme People's Court shall be used into consideration in subsequent instances. If other courts share identical opinions as the First-instance Court, it will be difficult to rely on the fraud standard in Vietnam Civil Law to apply the fraud rules or to delay the bank's payment obligation under the letter of credit. To protect the truthful parties, the court that agrees with the First-instance Court must have a stronger foundation about the deception in the letter of credit. Since UCP does not contain fraud provisions and this matter is treated as local law, defining fraud rules in the letter of credit laws for Vietnam's legal system may help Vietnamese judges who must define standards of fraud in the letters of credit in further cases feel less frustrated. Additionally, courts will have a foundation from which to work if a case involving fraud in letters of credit arises. This might also help to reduce instances of letter of credit procedural breaches. There is a chance that the judges will disregard the letter of credit transaction process, which will have a negative effect on the stability of letters of credit as well as the Vietnamese banking system. Judges are knowledgeable, but not all of them have expertise in a particular area, such as letters of credit

As has been mentioned, fraud rules of the US and the P.R.C. is well-drafted and meet the demands of the banking industry as well as preserve the commercial utility of letters of credit. Referring to such regulations shall help the lawmakers in Vietnam have a broader view of the mechanism and set a good foundation for fraud rules in the Vietnamese legal system. However,

while the basic principles of the fraud rule are similar in the US and P.R.C., there are some differences in how the rule is applied and enforced in these two countries.

For Vietnam, referring to the fraud rules of the United States and P.R.C. is necessary because the United States and P.R.C. are both the biggest financial centres, whereas the United States owns enormous cases of law which is very useful to consult. Since both the United States and P.R.C. have regulations related to fraud rules, they experienced specific problems which lawmakers in Vietnam should avoid. For example, the lawmakers for the letter of credit law in Vietnam should appreciate the international practice in the international rules like the drafters of Revised Article 5 of the Uniform Commercial Code of the USA have done since they adopt the UCP's approaches as well as their language (Barnes, 1996). The commentaries in Revised Article 5 extend the knowledge of the judges about letters of credit and firmly state to the judges that the fraud rules are extraordinary and should be issued with clear legal remedies (Blodgett & Mayer, 1998, p. 457). This spirit needed to be embodied in the Vietnam fraud rules since the courts tend to protect the defrauded parties and viable legal remedies are being used widely. The courts are encouraged to refer to international practice more than just look up the solutions in the law. The adoption and implementation of the law for fraud prevention and detection in Vietnam can increase the trust and confidence of foreign partners and investors in the Vietnamese market, leading to more opportunities for trade and investment and greater access to global resources and networks. The alignment of fraud rules with international norms and guidelines can improve the transparency and predictability of the legal and regulatory environment in Vietnam, promoting a culture of compliance and ethical behaviour and reducing the risk of reputational damage and legal liabilities for Vietnamese businesses.

However, since the Vietnam Commercial Law is drafted with different scopes from the UCC, having the Commercial Law redrafted and adding new articles with fraud rules seems unreasonable. Fraud rules in Vietnam must consist of essential elements such as the independent principle, the standards of fraud, the exemption of the fraud exception, the procedure regarding the remedies of the courts as well as the rights of parties in applying for remedies, etc. These features cannot be all drafted in the Vietnam Commercial Law. In such circumstances as well as considering Vietnam's economic situation, a by-law document issued by the Supreme People's Court of Vietnam which is similar to the 2005 Rules of the P.R.C. is justifiable. From this point of view, a Judicial Interpretation issued by the Supreme People's Court of Vietnam on the legal interpretations of the fraud rules should be considered. The Vietnam Supreme People's Court should prepare specific instructions for several situations including specific cases to particular rules or peculiar guidance in special fields that the law has not reached. The Judicial Interpretation of Vietnam must cover the entire letters of credit area, but its main target is the fraud rules and focuses on problem-solving rather than issuing a statute for a letter of credit. In general, the Judicial Interpretation of Vietnam includes both procedural and substantive matters of the letter of credit law. There are some features that the Judicial Interpretation should consider:

- Fraud standards

Fraud rules are unique because they are exceptions to the main principle of letters of credit- the independent principle. An approach to fraud rules will create a stable apportionment of the risks facing each of the parties (Houten, 1984, p. 385). To establish the standards in a complex area like fraud rules, the legislators need to prepare specific regulations to create a stable system. The standard must not be either too high or too low. The functions of the letter of credit must be kept while the courts still find the fraud rules are reasonable to apply. Frankly saying, it is very hard to build legal rules to govern fraud in letters of credit.

The standards should be drafted straightforwardly and define the misconducts that can appeal to the fraud rules. By giving a clear and narrow scope to the fraud rules, the Judicial Interpretation would provide good guidance to the courts to apply the fraud rules without being afraid of interfering with the international practice of letters of credit. It is recommended that the standards should be a "narrowly gauged standard" and "not just any fraud will suffice" (Task Force, 1990). The Vietnam lawmakers could consult the fraud standards in the Revised Article 5, Section 5-109 of UCC. The standard is now known as "material fraud", this definition has tackled the most opinionated issues in Previous Article 5. However, Section 5-109 has not defined "material fraud". The location of fraud is identified as the fraud could be in the documents or the underlying transaction (Uniform of Commercial Code, 1952, Section 5-109).

The 2005 Rules of P.R.C. also propose an interesting view about the fraud rules that lawmakers should consider. The 2005 Rules do not impose the general standards as the UCC, but it lists exact situations that fraud rules could be invoked. With this point of view, the applicants and the courts in Vietnam could consult the frameworks easier since Vietnam is a civil law country, and the courts prefer to consult the code than other sources.

From my point of view, both approaches are reasonable, but the approach of Chinese law seems to have a better fit for the commercial situations in Vietnam. The Vietnamese People's Courts could refer to the situations in the Judicial Interpretation to have a good overview of circumstances rather than consulting the fraud standards like the US courts. The disadvantage of following the UCC is it will create several standards which might confuse the merchants and the banks.

- The holder in due courses:

The beneficiary always wants to get payment in his currency, so he usually requires receiving money from a local bank. This feature also creates the commercial benefit of letters of credit since the local banks can give bits of advice, accept, and honour the presented documents, and from the point of view of the beneficiary, the correspondent bank stands in the same position as the issuing bank. These local banks will struggle with losses if fraud is involved in letters of credit because due to the independent principle, they are not allowed to look beyond the submitted documents and discover fraudulent activities. Hence, having exemptions for these innocent parties should be sincerely recognized when drafting fraud rules. If the innocent parties are not protected, these local banks will hesitate in taking part in letters of the credit

process. The lack of local banks will let the beneficiary uncertain about letters of credit and reduces the economic utility.

In my opinion, under the guidance of the international rules, references from Article 5 of UCC and the 2005 Rules of P.R.C, the innocent third parties should be listed as the nominated person or the person authorized by the issuing bank, the confirming bank, the holder in due courses and the assignee of deferred payment with good faith.

- The nominated persons by the issuer: the issuing bank sometimes can nominate a person as their representative in letters of credit. In this circumstance, this person, even though he is considered an agent of the issuer, is the issuer from the orientations of other parties. Hence, once this person honours the documents with good faith, they must be reimbursed under letters of credit regardless of fraudulent activities.

- Confirming banks: The issuer will authorize a beneficiary's local bank to honour the documents, this local bank is called confirming bank. The confirming bank stand in the same position as the issuing bank within the view of the beneficiary. The confirmer must be protected from the fraud rules if they honour the documents with good faith. The confirming bank is also put in an uneasy situation that whether he should pay the beneficiary since the confirmer is afraid of losing reimbursement from the issuer if the documents presented are the subject of the injunction. Otherwise, the confirming bank may be recognized as breaching the contract with the beneficiary if they decline the payment.

- The holder in due courses: the holder in due courses is known as the person who honours the documents with good faith before the injunction and he must not know about the fraud. The holder in due course is recognized that he must be preserved in case of the fraud rules are invoked. This exemption is considered under the Sztejn case (Sztejn v. Henry Schroder Banking Corp. , 1941).

- The assignee of deferred payment obligation: the beneficiaries always want to get the payment as quickly as possible once they submit the documents. Sometimes, they will ask a bank to advance part or all the funds under the deferred payment obligation with a discount. This bank is known as an assignee. Hence, once the assignee honours the documents with good faith, he should be protected from the fraud rules.

As we can see, the banks which fall into the category holders in due course may recover from the maker or drawer notwithstanding defects in the underlying transaction that generated the documents. These banks might find themselves being in litigations raised by the beneficiary in case they reject the presented documents. A correspondent bank should not take any risks by dishonouring the documents in doubt of fraud. If the presented documents "on their face" conform with the terms and conditions of the letter of credit, the correspondent bank shall pay. They do not obtain the risk of not receiving reimbursement from the issuer in case of fraud. Hence, these banks shall not risk their reputation in international trade to reject the submitted

documents in case there are allegations of fraud in the letter of credit as long as they still get their reimbursement.

In letters of credit, the bank offers some type of "verification" of data that it can evaluate better compared to the other participants of the transaction as a matter of transactional nature (Mann, 2000, p. 2521). In my opinion, the issuer's tacit validation of the applicant's dependability and respectability while issuing the letter of credit explains the prevalent use of letters of credit. Such verification, technically, is a typical example of reputational intermediaries: the applicant/buyer "rents" the issuer's reputation in order for the beneficiary/seller to check the reliability of the applicant/buyer to pay when the seller sends the items. The existence of a reputational consequence against the bank that gives the letter of credit fundamental to that arrangement (Mann, 2000, p. 2521). Hence, to the banks, especially the issuing bank, their strong reputation is important in letters of credit (Mann, 2000, p. 2525). The banks shall choose their credibility over things (Mann, 2000, p. 2525) and pay letters of credit then they are supposed to be paid[152].

- Definition of good faith

Good faith is a crucial part of fraud rules. Fraud rules will not be applied if the complied documents are submitted by the holder in due course with good faith. This element should be seriously considered since the intention of the fraud rules is not only to protect the economic benefit of the credits but also to protect the innocent parties.

Vietnamese lawmakers must add good faith in the drafting of fraud rules because the definition of good faith will complete fraud rules. Under the Vietnamese Civil Code 2015, there is no fixed definition of good faith. In the light of Article 3.3 of Civil Code 2015, good faith is only recognized as follows:

> "Each person must establish, exercise/ fulfil, or terminate his/her civil rights and/or obligations in the principle of good faith and honesty."

As stated above, the law in Vietnam's Legal System does not have a specific definition of good faith as the common law countries. Hence, the author suggests that lawmakers should examine the definition of good faith by consulting the definition of good faith under Article 5 of the UCC. The first definition of good faith is "observance of reasonable commercial standards of fair dealing" in Section 1-201(19)[153] and this observance is applied through all commercial transactions. The second definition could be observed as "honesty in fact"[154] from Section 1-

[152] "They are supposed to be paid" means the presented documents on its face conform to the requirements in the letter of credit.
[153] Article 1-201-19 of UCC provides:
Every contract or duty within this Act imposes an obligation of good faith in its performance or enforcement.
[154] Article 1-203 of UCC provides:
Good faith in a case of a merchant means honesty in fact and the observance of reasonable commercial standards of fair dealing in trade.

203 of UCC (Uniform of Commercial Code, 1952) by following the reasonable commercial standard by merchants (Symons, 1979-1980, p. 349).

Another definition that the Vietnamese lawmakers could consult is the definition of the 2005 Rules of Chinese Law. In the light of Article 10 of the 2005 Provisions, good faith must be understood as "without notice of fraud" (Gao, 2007, p. 1083). Concerning the position of the confirming bank, good faith should be defined a little bit differently. Normally, the confirming bank barely dishonours the conforming documents since they will be accused by the beneficiary, and they might be in trouble. Considering the special position of the confirming bank, good faith must be understood without any secret understanding of the fraud (Gao, 2007, p. 1083).

- Remedy of the Courts

As we have seen, in Case Law 13/2017/AL, the applicant inquired the court to issue injunctive relief to stop the payment obligation of the buyer based on a breach of warranty. This behaviour is serious since it violates the interest of the seller. The case law also shows the possibility of the court cancelling the credit because the court believes that the letter of credit is an integral part of the contract and when the contract is cancelled, so is the letter of credit. The process of letters of credit is easy to abuse, which leads to difficult circumstances for domestic banks and foreign banks in the process of letters of credit, especially when the banks honour the documents with good faith.

Having regulations related to the restraining order or issuing an injunction would lift the burden of the banks to have their reputations affected. The international reputation of the banks will be affected if the process of letters of credit keeps being interfered with by the courts in Vietnam. The Judicial Interpretation should propose different remedies to apply once fraud is found in the transactions. For example, the temporary remedy to postpone the payment before seriously considering the case or the permanent remedy which could be applied after the full trial court is worth considering.

- Parties applying for Court's remedies and the Court's jurisdiction

In drafting fraud rules for Vietnam law, Vietnamese lawmakers should consider who could apply for the injunction. The author believes that once fraud is found in the credit, the applicant, the issuer or the third parties who have interests affected could apply for an injunction from the courts. The applicant, the issuer, or the third parties who have an interest be harmed also could apply for the injunction under the guidance of Article 469 and Chapter III in the Civil Procedure Code 2015 (The National Assembly, 2015). They need to bear the burden of proof if they want to enjoin the process of letters of credit by claiming there is fraud. However, the chance of an issuing bank applying for an injunction might be limited since they might hesitate in asking the court to stop their payment because this behaviour will affect their international reputation.

However, in my opinion, in case of fraud is clear in the letter of credit, the issuing bank could take appropriate action to protect the interests of all parties involved. This may include notifying the buyer of the suspected fraud, rejecting any fraudulent documents submitted by the seller or applying for Court's remedy. It is important for the issuing bank to act quickly and decisively in response to fraud in order to minimize the potential harm to all parties involved and to maintain confidence in the letter of credit system. Overall, the issuing bank plays a critical role in detecting and preventing fraud in the letter of credit transactions and should take all necessary steps to protect the integrity of the system and the interests of all parties involved.

- The Ruling of the Court:

The courts must behave expeditiously when they receive the allegations from the applicant. I believe that these rules should be extracted from the Vietnam Civil Procedure Code. The late action of the courts might affect the economic benefit of letters of credit and the issuing bank will be put in a dilemma situation. If the issuing bank refuses to honour the documents based only on the claim of the applicant, their international reputation might be harmed. So, the injunction from the court might help to smooth the situation.

- Reconsideration for the Ruling of The Court

In Case Law 13/2017/AL and other cases, there might be chances that parties find the judgment in payment suspension is not proper, in that case, they can apply to a higher People's Court to reconsider the judgment. This substance is needed depending on the special feature of letters of credit and the current situation in Vietnam law. The parties in Vietnam have 15 days to appeal to the next higher people's court to have their ruling reconsidered since the date of the judgment of the first instance court (The National Assembly, 2015)[155]. However, the letter of credit is a special instrument that requires a faster procedure. The Judicial Interpretation should express their concern over the special features of letters of credit and having a shorter as well as reasonable period for the appellation. Such Judicial Interpretation will soothe the banks' minds since they will no longer worry about their reputation in international trade because of the delay in paying.

[155] Article 280 of the Code of Civil Procedure 2015: Time limit for an appeal
1. The time limit for making an appeal against a first-instance court's judgment shall be 15 days for the procuracy of the same level and 1 month for the immediate superior procuracy, counting from the date of judgment pronouncement. In cases where the procurators do not attend the Court sessions, the appeal time limit shall be counted from the day on which the procuracy of the same level receives the judgment.
2. The time limit for making an appeal against the first-instance court's decision on suspension or termination of the resolution of the case shall be 07 days for procuracy of the same level and 10 days for immediate superior procuracy, counting from the day on which the procuracy of the same level receives such decision.
3. If the Court receives the appeal decision from the procuracy after the time limit prescribed in clauses 1 and 2 of this Article, the first-instance Court shall request the procuracy to provide explanation in writing.

CHAPTER X

CONCLUDING REMARKS

For several years, merchants always desire to reduce their risk while entering international transactions. Since international transactions require transportation over borders, the differences in legal systems, languages, cultures, etc., have more risks than domestic ones. To protect their benefits and their commercial interests, the merchants have tried to invest in several methods to save themselves from the hazard of international trade. One of the methods which gain the trust of the merchants is the commercial letter of credit. This mechanism has a unique process. Its history has a close relation to other negotiable instruments, particularly bills of exchange, and the letter of credit remains its speciality in the universal organization. The letter of credit gives the seller in the transaction guarantee for payment while protecting the buyer from improper demands.

The banking practice has a strong effect on the letter of credit law, and it has developed together with international customs. Such customs are organized and institutionalized into a set of regulations issued by the International Chamber of Commerce which is called the Uniform Customs and Practice for Documentary Credits. This uniform is accepted and observed throughout the world by the banking industry, making UCP become the most outstanding set of rules in harmonizing universal practice regarding letters of credit. The UCP is considered the main source of the law of letters of credit. Besides the UCP, the thesis has mentioned other sources the UNCITRAL Convention 1995, which is drafted by the United Nations. Alongside UCP, the UNCITRAL Convention 1995 has contributed to shaping the law of letters of credit and fraud rules.

The inter-relationships in letters of credit are created by complex relations between the seller, the bank, and the buyer. Such relations as well as the rights and duties of each party are described and explained in the thesis. The requirements, as well as the banks' obligations, are also well analysed, along with the requirements of letters of credit. The main concern of the banks in letters of credit is the documents, hence, examining the goods do not fall into their category. Thanks to the Independent principle and the Strict Compliance principle, letters of credit could keep their unique nature which is providing a safe and stable mechanism for international trade. Due to the strict observance of the independent principle, the process of letters of credit runs smoothly and the seller is protected from the allegations raised by the buyer in the underlying contract. At the same time, the Strict Compliance principle assures that the buyer only gets the documents that comply with the requirements of the credit.

However, there are always unscrupulous people who try to abuse the system. The concern of the banks with the documents is whether the documents are forged or are made up to comply with the requirements and do not reflect the real goods. The exception of the independent principle, fraud rules, allows the courts to look beyond the documents and investigate the factual situations in the sales contract. Such fraud rules are still being developed and have

several arguments. The courts have developed several standards regarding the payment obligation of the banks when fraud is invoked. The fraud "gap" which is left by the UCP becomes the alternative intimidation to the stable of letters of credit. After the UCP 600, the ICC keeps silent about the fraud exception and remains its opinion that the fraud exception belonged to national provisions. Hence, some countries have tried to embed fraud rules into their domestic law such as the United States or the Republic of China. Their fraud rules are explained and clarified in the thesis which creates a good example to consult for Vietnam in creating its own fraud rules.

Alongside the development of Vietnam's economy, fraudulent activities also increase. Without fraud rules for letters of credit in Vietnam's legal system, the commercial utility of letters of credit might be threatened. The applicant might try to take advantage of this loophole and stop the payment of the banks even if there is only a breach of the warranty in the sales contract. The situation in Vietnam legislation is partly illustrated through Case Law No. 13/2017/AL. Even though this case law is not enough to represent the whole scenario in Vietnam, however, it is still valuable to consider.

In my opinion, having fraud rules in the letter of credit law is an essential element of any legal system that seeks to promote fair trade and protect the interests of all parties involved in international transactions. A letter of credit is a financial mechanism that serves as a guarantee of payment between a buyer and a seller in a commercial transaction, and it is widely used in international trade to minimize the risk of non-payment or other contractual breaches. However, as with any legal document or contract, there is always the possibility of fraud or misrepresentation, either by the buyer or the seller. In such cases, fraud rules are necessary to ensure that the innocent party is not unfairly penalized and that the fraudulent party is held accountable for their actions. A fraud rule in national law can help to provide a legal framework for addressing and preventing fraudulent activities, which can protect merchants and promote a healthy and transparent business environment. Without a fraud rule in place, there would be a significant risk of abuse and exploitation in international trade, which could lead to financial losses and damage to the reputation of the parties involved. Furthermore, fraud rules help to ensure that the legal system can effectively enforce the terms of the letter of credit, which is crucial for maintaining confidence in international trade. A fraud rule in national law can also help to deter fraudulent activities by establishing penalties and consequences for those who engage in fraudulent behaviour. This can serve as a powerful deterrent to potential fraudsters, as they will know that they could face legal action if they engage in fraudulent activities. In addition, a fraud rule can help to provide merchants with a sense of security and confidence when conducting business, as they will know that the legal system is available to help protect their interests.

Furthermore, a fraud rule in national law can promote a level playing field for all businesses, as it helps to ensure that all parties are held accountable for their actions. This can help to prevent unfair competition and promote a healthy and transparent business environment that benefits both merchants and consumers. It is essential for protecting merchants and promoting a healthy and transparent business environment. It can help to deter fraudulent activities,

provide merchants with a sense of security and confidence, and promote fair competition among businesses. I believe that fraud rules are a necessary and important aspect of the letter of credit law, and any legal system that seeks to promote fair and equitable trade should include such a provision in its regulation

From the author's perspective, Vietnam should have a good Judicial Interpretation which contains fraud rules in commercial letters of credit. This Judicial Interpretation shall guide the People's courts to deal with fraud and educate them about the importance of the financial stability of letters of credit and how to define and deal with fraud in letters of credit. The author strongly supports a new Judicial Interpretation regarding the fraud rule for letters of credit in Vietnam provisions. The failure to keep the stability of letters of credit might lead to gradual erosion, which affects the reputation of not only the banking system in Vietnam but the Vietnam courts.

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