THE EFFECT OF UCP 600 UPON U.C.C. ARTICLE 5 WITH RESPECT TO NEGOTIATION CREDITS AND THE IMMUNITY OF NEGOTIATING BANKS FROM LETTER-OF-CREDIT FRAUD

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I. INTRODUCTION

> This inquiry [the definition of negotiation credit] is plagued by confusion over usage of the term "negotiation" and its cognates in various contexts. The drafters of the Uniform Commercial Code, the drafters of the Uniform Customs and Practice for Documentary Credits, and the banking industry itself use those terms inconsistently.[1]

Under U.C.C. Article 5,[2] a documentary letter of credit is a definite undertaking by the issuer, which typically is a financial institution, to the beneficiary to honor a required documentary presentation.[3] If the issuer and the beneficiary operate in different markets, a common situation with respect to international sales of goods, the beneficiary, the seller in the underlying sale transaction, usually prefers to obtain payment from a local financial institution. One way in which a distant issuer can accommodate the beneficiary is by issuing a "negotiation credit." A "negotiation credit" authorizes one or more financial institutions to purchase from the beneficiary the documents required by the issuer's letter of credit and to present those documents to the issuer for reimbursement.[4] However, the usefulness of negotiation credits has been impaired by dissonance with respect to what constitutes negotiation.[5]

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1. John F. Dolan, *Negotiation Letters of Credit*, 119 BANKING L.J. 409, 410 (2002).

2. The Official Text of the 1995 revision of Article 5, §§ 5-101 to 5-118, 2B Part II U.L.A. 136-88 (Master ed. 2002) [hereinafter cited as U.C.C. art. 5 Section Number]. The Official Text of the prior 1962 version, §§ 5-101 to 5-117, *id.* at 199-384 [hereinafter cited as 1962 U.C.C. art. 5 Section Number]. The 1995 revision of Article 5 has been enacted in every state. *See* National Conference of Commissioners on Uniform State Laws, U.C.C. Article 5—Letters of Credit, *available at* http://www.nccusl.org/Update/-uniformact_factsheets/uniformacts-fs-ucca5.asp (last visited Nov. 18, 2008).

3. U.C.C. § 5-102(a)(10) ("'[L]etter of credit' means a definite undertaking . . . by an issuer to a beneficiary at the request or for the account of an applicant . . . .").

4. *See* Robert M. Rosenblith, *Litigating the Letter of Credit Case—Liability of Banks Under the Current and Revised Uniform Commercial Code*, 33 UCC L.J. 131, 158 (2000) ("The issuer states to a negotiating bank: 'I am obligated to pay the beneficiary without recourse if he presents the required documents to me. . . . If you make the payment to the

This article discusses the current status of negotiation credits under the three principal regimes of American letter-of-credit law: U.C.C. Article 5 (Article 5),[6] the 2007 Revision of the Uniform Customs and Practice for Documentary Credits (UCP 600),[7] and the 1998 International Standby Practices (ISP 98).[8] The most important of these regimes is UCP 600. Article 5 defers to the incorporation of most conflicting UCP rules into a letter of credit[9] and most negotiation credits

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beneficiary that I would be obligated to make if the beneficiary had presented to me, I will reimburse you without recourse to you.'").

5. *See, e.g.*, Dolan, *supra* note 1, at 409-10 (contending that banks nominated to negotiate are not truly negotiating).

6. *See* discussion, *supra* note 2.

7. INT'L CHAMBER OF COMMERCE (ICC), UNIFORM CUSTOMS & PRACTICE FOR DOCUMENTARY CREDITS 2007 REVISION, at title page (ICC Pub. No. 600 2006) [hereinafter UCP 600]. The UCP 600 Drafting Group has published an article-by-article analysis of UCP 600. *See* INT'L CHAMBER OF COMMERCE, COMMENTARY ON UCP 600 (ICC Pub. No. 680 2007) [hereinafter DRAFTING GROUP COMMENTARY UCP 600]. The ICC is a world business organization with members in over 130 countries. *See* UCP 600, *supra*, at 69. Bankers in most countries and in every major financial center rely upon the UCP. *See* James E. Byrne, *Fundamental Issues in the Unification and Harmonization of Letter of Credit Law*, 37 LOY. L. REV. 1, 3 n.5 (1991) (noting that the UCP has achieved virtual universal adherence). The operative version of the UCP is revised and renumbered periodically—UCP 500 preceded UCP 600. *See* ICC, UNIFORM CUSTOMS & PRACTICE FOR DOCUMENTARY CREDITS 54 (ICC Pub. No. 500 1993) [hereinafter UCP 500]. In 2003, the ICC published a partial compilation of international standard banking practice under UCP 500. *See* ICC, INT'L STANDARD BANKING PRACTICE (ISBP) (ICC Pub. No. 645 2003). The ISBP did not amend UCP 500 and should not have been separately incorporated into a letter of credit. Its function was to clarify the significance of incorporation of UCP 500. *Id.* at 8-9 (stating that the ISBP explains rather than amends UCP 500 and its incorporation into a letter of credit is discouraged). The ICC has updated and conformed the ISBP to UCP 600. *See* ICC, INT'L STANDARD BANKING PRACTICE (ICC Pub. No. 681 2008).

8. *See generally* JAMES E. BRYNE, THE OFFICIAL COMMENTARY ON THE INTERNATIONAL STANDBY PRACTICES (Inst. Int'l Banking L. & Pract. 1998) [hereinafter OFFICIAL COMMENTARY ISP 98]. ISP 98 is ICC Pub. No. 590. *See* discussion and accompanying text, *infra* notes 12-17 (discussing the concept of a standby letter of credit). The development of ISP 98 was coordinated by the nonprofit Institute for International Banking Law & Practice and the International Financial Services Association, an association of the major banks issuing letters of credit. *See* OFFICIAL COMMENTARY ISP 98, at xvi. ISP 98 has been endorsed by the ICC. *See id.* at v (preface by Dieter Kiefer). Professor James E. Byrne of George Mason School of Law, the Director of the Institute of International Banking Law & Practice, was Reporter and Chair of the Working Group for ISP 98. *See* OFFICIAL COMMENTARY ISP 98, *supra*, at 354. For more information on the Institute, *see* http://www.iiblp.org/ (last visited Nov. 18, 2008).

9. U.C.C. §§ 5-103(c), 5-116(c) (stating that, with the exception of the nonvariable U.C.C. provisions listed in § 5-103(c) and terms "generally excusing liability" and "generally limiting remedies," the liability of an issuer, a nominated person, and an advisor is governed by rules of custom and practice like the UCP to which a letter of credit, a confirmation, or other undertaking is expressly made subject). The nonvariable

are the commercial letters of credit for which UCP 600 is designed rather than the standby letters of credit for which ISP 98 is appropriate.[10] The importance of UCP 600 is augmented by its potentially world-wide incorporation into commercial letters of credit.[11]

Article 5 provisions are: the definitions of "issuer" and "letter of credit," the conversion of "perpetual" letters of credit into letters of credit with a five-year duration, the statutory expression of the "Independence Principle," the prohibition upon an issuer or a nominated person unreasonably refusing to consent to an assignment of the proceeds of a letter of credit that must be presented for honor, the requirement that an issuer or a nominated person must have honored or otherwise paid a letter of credit in order to be entitled to statutory subrogation rights, and the nonvariability of the preceding rules. *See* U.C.C. § 5-103(c) (incorporating, expressly, the nonvariable provisions by reference). The fundamental U.C.C. obligations of good faith, diligence, reasonableness, and care also can not be disclaimed. *See* U.C.C. § 1-302(b), 1 U.L.A. 42 (Master ed. 2004); §§ 1-101 to 1-310 of Revised Article 1, 1 U.L.A. 9-52 (Master ed. 2004) [hereinafter cited as U.C.C. art. 1 Section Number]. *See also* U.C.C. § 5-103(c), 1 U.L.A. 42 (Master ed. 2004) (cross-referencing §1-302); Sandra Stern, *Varying Article 5 of the UCC by Agreement*, 114 BANKING L.J. 516, 517-21 (1997) (discussing nonvariable provisions). But, a letter of credit can include agreed standards for these fundamental obligations that are not manifestly unreasonable. *See* U.C.C. §1-302(b), 1 U.L.A. 42 (Master ed. 2004) (stating that agreed standards can be permissible). The definition of letter of credit, *see* U.C.C. § 5-102(a)(10), is one of the Article 5 provisions that cannot be varied by either a contrary agreement or an incorporation by reference. *See id.* § 5-103(c) ("With the exception of . . . the effect of this Article may be varied by agreement or by a provision stated or incorporated by reference in an undertaking."). An attempt by the parties to vary the statutory definition of "letter of credit" by including nondocumentary conditions of honor could disqualify the undertaking from treatment as a letter of credit. *See, e.g.*, Wichita Eagle & Beacon Publ'g Co. v. Pacific Nat'l Bank, 493 F.2d 1285, 1286-87 (9th Cir. 1974) (stating that nondocumentary conditions with respect to external facts required enforcement of an instrument as a guaranty rather than as a letter of credit). *See generally* Richard F. Dole, Jr., *The Essence of a Letter of Credit under Revised U.C.C. Article 5: Permissible and Impermissible Nondocumentary Conditions Affecting Honor*, 35 HOUS. L. REV. 1079 (1998).

10. *See* Dolan, *supra* note 1, at 411-22 (using a commercial letter of credit transaction to illustrate a negotiation credit). *But see* OFFICIAL COMMENTARY ISP 98, *supra* note 8, rule 2.04, cmt. 1 ("It is not uncommon for a person (almost always a bank) to be nominated in the standby to advise, confirm, pay a presentation, effect a transfer, or negotiate a presentation made under a standby . . . ."). *See* discussion, *infra* notes 12-17 (distinguishing between a commercial and a standby letter of credit).

11. UCP 500, for example, has been the subject of numerous court decisions in the United Kingdom and the Commonwealth. *See, e.g.*, Banco Santander v. Bayfern, Ltd., [2000] 1 All E.R. (Comm) 776, 783-85 (C.A.) (analyzing UCP 500 provisions). A number of these court decisions relevant to UCP 600 are discussed in this Article.

II. OVERVIEW OF LETTER OF CREDIT LAW

A. The Distinction Between Commercial and Standby Letters of Credit

1. Article 5

Letters of credit conventionally are classified as either commercial letters of credit or standby letters of credit.[12] A commercial letter of credit requires the issuer to pay the seller of goods upon the seller's timely presentation of the documents specified in the letter of credit. The specified documents evidence the seller's performance of the agreed sale, and, in addition to the seller's draft[13] or demand for payment, typically include at least the seller's invoice and transportation documents indicating that the goods have been shipped.[14] Additional documents can be required, including a packing list, an insurance policy, an inspection certificate by an independent testing agency, a certificate of origin, and a certificate of shipment.[15]

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12. *See* JOHN F. DOLAN, THE LAW OF LETTERS OF CREDIT: COMMERCIAL AND STANDBY CREDITS 1-1 (rev. ed. 2003) (discussing standard letter of credit transactions) [hereinafter DOLAN TREATISE].

13. A draft is an order to pay money that is subject to U.C.C. Article 3 if it is in negotiable form. Revised art. §§ 3-101 to 3-605, 2 U.L.A. 23-354 (Master ed. 2004) [hereinafter cited as U.C.C. art. 3 Section Number]. *See, e.g.*, U.C.C. § 3-104(a), (e) (explaining that a draft is an order to pay money). The person who signs a draft is the "drawer." *See* U.C.C. § 3-103(a)(5) (stating that the drawer signs a draft). The person ordered to pay is the "drawee." *See* U.C.C. § 3-103(a)(4). Drafts in negotiable form are subject to U.C.C. Article 3 on negotiable instruments. *See* U.C.C. § 3-102(a) (stating that Article 3 applies to negotiable instruments). A draft utilized in conjunction with a letter of credit typically is drawn by the beneficiary as drawer upon the issuer or a confirmer as drawee, and may or may not be in negotiable form and subject to Article 3. *See* U.C.C. § 5-102, cmt. 11 ("[A] document may be a draft under Article 5 even though it would not be a negotiable instrument [under Article 3]."). If there is a conflict between Article 3 and Article 5, Article 5 governs. *See* U.C.C. § 5-116(d).

14. *See, e.g.*, S.B. Int'l, Inc. v. Union Bank of India, 783 S.W.2d 225, 226 (Tex. App. 1989) (involving commercial letter of credit requiring presentation of drafts, invoices, and bills of lading). In order to be timely, presentation must be made before both the expiration date and any earlier special document presentation deadline imposed by the letter of credit. *See* Banco General Runinahui v. Citibank Int'l, 97 F.3d 480, 483 (11th Cir. 1996) (involving letter of credit requiring all the documents to be presented: "no later than 15 days after shipment, but within the validity of the credit").

15. *See, e.g.*, Bank of Cochin v. Mfgs. Hanover Trust Co., 612 F. Supp. 1533, 1535 (S.D.N.Y. 1985), *aff'd*, 808 F.2d 209 (2d Cir. 1986) (involving commercial letter of credit requiring presentation of a certification by the beneficiary that it had performed the conditions of the letter of credit, a certification by Lloyd's of London or the shipping company that the ship was a first class or approved non-Pakistani vessel, a certificate of West European origin, a certificate of analysis by Lloyd's of London or another

All other letters of credit should be regarded as standbys.[16] Standby letters of credit can be used in any context, including sales, and are not limited to assuring payment in the event of default.[17] Notwithstanding these rules-of-thumb, distinguishing between commercial and standby letters of credit can be difficult, and also can be unnecessary. Article 5 adopts a "one law for all letters of credit approach." There are no special Article 5 rules for either commercial letters of credit or standbys.[18] Although UCP 600 is focused upon commercial letters of credit and ISP 98 upon standbys,[19] neither contains precise definitions.[20]

2. The Other Regimes

UCP 600 is a codification by the International Chamber of Commerce (the ICC) of the international standard practice of financial institutions that regularly issue commercial letters of credit.[21] UCP 600 is

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international testing agency, a marine insurance policy, and a packing list in addition to drafts, invoices, and bills of lading).

16. JAMES G. BARNES, ET AL., THE ABCs OF THE UCC ARTICLE 5: LETTERS OF CREDIT 1-10 (Boss ed. 1998) [hereinafter BARNES ET. AL.] (noting that, although both standby and commercial letters of credit "provide for payment against the presentation of specified documents," standbys do not require "a negotiable bill of lading or other transport document"; also noting the varied uses of standbys, including providing cash collateral upon the immanent expiration of a letter of credit that neither has been renewed nor replaced).

17. *See id.* at 7-9 (contending that it is false to imply that a standby letter of credit is payable only after a default or is not used in sales of goods). Nevertheless, standby letters of credit are used frequently to assure payment in the event of the applicant's default; *see, e.g.*, Interfirst Bank Greenspoint v. First Fed. Sav. & Loan Ass'n, 747 P.2d 129, 131-32 (Kan. 1987) (involving standby letter of credit requiring presentation of sight draft, signed certificate that named individuals had not performed satisfactorily under the terms of a contract or other obligation to Interfirst Bank Greenspoint or its transferee, plus the original letter of credit).

18. BARNES ET AL., *supra* note 16, at 9 ("[T]he one law for all letters of credit approach [is] taken in UCC Article 5.") (quotation omitted).

19. *See* discussion and accompanying text, *infra* notes 24-30.

20. *See* UCP 600, *supra* note 7, art. 2 (8th definition) ("Credit means any arrangement, however named or described, that is irrevocable and thereby constitutes a definite undertaking of the issuing bank to honour a complying presentation."). UCP 600 applies to all Credits, including standby letters of credit, that incorporate it. *See id.* art. 1 ("[These] rules . . . apply to any documentary credit ("credit") including, to the extent that they may be applicable, any standby letter of credit when the text of the credit expressly indicates that it is subject to these rules."); OFFICIAL COMMENTARY ISP 98, *supra* note 8, rule 1.01, cmt. 3, at 2 (providing no definition of a standby letter of credit); *see also id.* cmt. 9, at 4 (explaining that the phrase "documentary letter of credit" is avoided because it is ambiguous).

21. *See* ICC, DOCUMENTARY CREDITS: UCP 500 & 400 COMPARED III (ICC Pub. No. 511 Charles del Busto ed., 1993) (comparing UCP 400 and UCP 500) [hereinafter UCP

not law per se[22] but is enforced by courts and arbitration tribunals as part of the undertaking of an issuer that has incorporated UCP 600 into its letter of credit.[23] UCP 600 is designed for commercial letters of credit.[24] Substantial adjustments must be made for UCP 600 to be appropriately incorporated into a standby.[25]

The focus of UCP 500, the version that preceded UCP 600,[26] upon commercial letters of credit[27] led to the ICC's endorsement of ISP 98 for standby letters of credit.[28] Like the UCP, ISP 98 is incorporated into a letter of credit and enforced as part of the issuer's undertaking.[29] ISP 98 is not designed for commercial letters of credit.[30]

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500 & 400 COMPARED] (discussing the role of the ICC and presenting a justification for UCP 500). *See supra* note 7 (discussing the ICC).

22. *See* UCP 500 & 400 COMPARED, *supra* note 21, at 2 (noting that incorporation of the UCP is subject to national law and that courts and arbitration tribunals must resolve conflicts with national law).

23. *See, e.g.*, San Diego Gas & Elec. Co. v. Bank Leumi, 50 Cal. Rptr. 2d 20, 24-25 (Ct. App. 1996) (stating that the UCP has the force of law with respect to a letter of credit incorporating it).

24. *See* OFFICIAL COMMENTARY ISP 98, *supra* note 8, at vii ("To accurately reflect the . . . requirements of a standby, one would have to exclude, amend, or adapt the majority of the articles in the UCP.").

25. UCP 600, *supra* note 7, art. 1 (stating that UCP 600 applies to any Credit in which it is incorporated, including, to the extent applicable, standbys). *See, e.g.*, E & H Partners v. Broadway Nat'l Bank, 39 F. Supp. 2d 275, 277-78 (S.D.N.Y. 1998) (involving standby letter of credit incorporating UCP 500). However, careful lawyers exclude inappropriate UCP 600 articles from incorporation into a standby; *see* James E. Byrne, *The International Standby Practices (ISP98): New Rules for Standby Letters of Credit*, 32 UCC L.J. 149, 155-58 (1999) (identifying UCP 500 articles that are "problematic" for standbys). Professor Byrne also discusses other provisions that would have been appropriate for standbys that are either "imprecise" or omitted from UCP 500. *Id.* at 158-62.

26. *See* discussion, *supra* note 7.

27. *See* discussion and accompanying text, *supra* notes 12-17 (describing a commercial letter of credit).

28. *See* OFFICIAL COMMENTARY ISP 98, *supra* note 8, at xvi (discussing the need for ISP 98); *supra* note 8 (describing ICC's endorsement of ISP 98); discussion and accompanying text, *supra* notes 12-17 (describing standby letter of credit).

29. *See* OFFICIAL COMMENTARY ISP 98, *supra* note 8, rule 1.04(i) (mandating that unless the context requires otherwise or ISP 98 expressly is modified or excluded, upon incorporation into a letter of credit, the terms and conditions of ISP 98 are part of the issuer's agreement).

30. *See* JAMES E. BYRNE, ISP98 & UCP500 COMPARED rule 1.01, cmt. 5 (Inst. Int'l Banking L. & Prac. 2000) ("[ISP98] was not designed for commercial letters of credit."). If the issuer of a letter of credit mistakenly incorporated both UCP 600 and ISP 98, the result could be surprising. UCP 600 has no rule dealing with conflicting incorporations but ISP 98 does. *See* OFFICIAL COMMENTARY ISP 98, *supra* note 8, rule 1.02(b) (indicating that ISP 98 supersedes conflicting rules of practice to which a standby letter of credit is subject). This carefully phrased statement means that incorporation of both

B. Article 5: General Definitions

Under Article 5, which measures time in "business days,"[31] a "letter of credit" is a definite and irrevocable[32] undertaking by the "issuer"[33] either to pay or to deliver an item of value upon satisfaction of the documentary conditions precedent to the issuer's duty to honor.[34] The issuer's definite undertaking is made to the "beneficiary"[35] at the request of, or for the account of, the "applicant."[36] The beneficiary, a nominated person, or a person, typically a bank, acting for the beneficiary or a nominated person that presents the required documents to the issuer for honor or reimbursement is the "presenter."[37]

UCP 600 and ISP 98 into a commercial letter of credit would not result in ISP 98 superseding UCP 600. To the extent that they are consistent, both would apply. *See id.* cmt. 6, at 10 (stating that rule 1.02(b) does not apply to conflicting rules applicable to a commercial letter of credit but to the extent they are consistent, both would apply).

31. *See* U.C.C. § 5-108(b) (requiring that the issuer either must honor or give notice of dishonor by the end of the "seventh business day" after the business day of receipt of the documents).

32. *See* U.C.C. § 5-106(a) (stating that a letter is revocable only if it so provides). There is no market for revocable letters of credit.

33. U.C.C. § 5-102(a)(9) (explaining that the "issuer" is the "person that issues a letter of credit"). In order to prevent a wily creditor from depriving an individual consumer of defenses to payment by requiring the consumer to issue a letter of credit naming the creditor as beneficiary, undertakings by individuals with respect to personal, family or household debts do not qualify as letters of credit. *See* U.C.C. § 5-102(a)(9) (providing that "issuer" does not include an individual engaged in a consumer transaction); U.C.C. § 5-102, cmt. 5 (noting that consumers are excluded from the definition of "issuer" in order to preserve their defenses against creditors).

34. *See* U.C.C. § 5-102(a)(10). The definition of letter of credit is one of seven Article 5 provisions that cannot be varied by either a contrary agreement or an incorporation by reference. *See* U.C.C. § 5-103(c) ("With the exception of . . . the effect of this Article may be varied by agreement or by a provision stated or incorporated by reference in an undertaking."). *See* discussion, *supra* note 9 (discussing nonvariable provisions).

35. Under the terms of the letter of credit, the "beneficiary" is the person who is entitled to have a complying presentation of documents honored. *See* U.C.C. § 5-102(a)(3).

36. The "applicant" is the person at whose request or for whose account the letter of credit is issued. *See* U.C.C. § 5-102(a)(2). An issuer that properly has honored a presentation of documents is entitled to be reimbursed by the applicant. *See* U.C.C. § 5-108(i)(1) ("[A]n issuer that has honored a presentation as permitted or required by [Article 5] is: (1) entitled to be reimbursed by the applicant in immediately available funds . . . ."). An issuer's statutory right to reimbursement typically is supplemented by a reimbursement agreement. *See, e.g.*, Gillman v. Chase Manhattan Bank, 534 N.E.2d 824, 826-27, 831 (N.Y. 1988) (involving a security agreement on the reverse of the signed letter of credit application entitling the issuer to deny the applicant access to its deposit accounts with the issuer).

37. *See* U.C.C. § 5-102(a)(13); *see, e.g.*, DBJJJ, Inc. v. Nat'l City Bank, 19 Cal. Rptr. 3d 904, 907-8 (2d Dist. 2004) (presenting documents to the issuer by a bank acting on

If the issuer and the beneficiary operate in different markets, the beneficiary typically prefers to obtain payment from a local financial institution. In order to facilitate this, the issuer can undertake to reimburse a designated "nominated person"[38] in the beneficiary's market for giving value pursuant to the issuer's letter of credit. A nominated person has no obligation to act upon its nomination.[39] But, a nominated person that also accepts the issuer's request to become a "confirmer"[40] undertakes to honor the presentation required by the issuer's letter of credit, assuming obligations to both the issuer and the beneficiary.[41] The confirmation of the issuer's letter of credit at the issuer's request is deemed to make the issuer an "applicant" for a letter of credit issued by the confirmer.[42] Article 5 enhances certainty of payment by imposing the same obligations upon issuers and confirmers.[43] Although confirmers are nominated persons,[44] in view of the marked differences between the obligations of confirmers and other nominated persons, "nominated person" and "nominated bank" will be used to refer to nominated persons that are not confirmers. Confirmers will be referred to as "confirmers."

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behalf of the beneficiary). *See* discussion and accompanying text, *infra* note 38 (explaining the concept of nominated person).

38. *See* U.C.C. § 5-102(a)(11) (stating that a nominated person is designated by the issuer who undertakes to reimburse the nominated person for giving value under the letter of credit).

39. U.C.C. § 5-107(b). Although a nominated person could agree to act upon its nomination, this agreement is not ordinarily required by the issuer. *See id.*

40. *See* U.C.C. § 5-102(a)(4) (defining "confirmer" as a "nominated person who undertakes, at the request or with the consent of the issuer, to honor the [issuer's letter] of credit"). A confirmer must have been designated or authorized by the issuer to give value under the issuer's letter of credit. *See id.* cmt. 1 (noting that a person that agrees to confirm without the designation or authorization of the issuer is not an Article 5 confirmer); U.C.C. § 5-102(a)(11) (defining "nominated person"). An unauthorized confirmer is referred to as a "silent confirmer." *See* Dibrell Bros. Int'l S.A. v. Banca Nazionale del Lavoro, 38 F.3d 1571, 1575-76, n.4 (11th Cir. 1994) (holding that silent confirmation occurs when the beneficiary rather than the issuer requests confirmation). A silent confirmer can have the Article 5 liability of an issuer of a letter of credit for its own account, or, if its undertaking does not qualify as a letter of credit, contractual liability to the beneficiary. *See* U.C.C. § 5-102, cmt. 1 (stating that a silent confirmer can be liable under either Article 5 or contract law).

41. *See* U.C.C. § 5-107(a) (noting that to the extent of its confirmation, a confirmer has rights and obligations with respect to the confirmed letter of credit as though it was the issuer and also has rights and obligations with respect to the issuer of the confirmed letter of credit as though the issuer was the applicant for the confirmed letter of credit).

42. *See id.*

43. *See* U.C.C. § 5-108, cmt. 1 (providing a confirmer has the same rights and duties as the issuer).

44. *See* discussion, *supra* note 40.

An "adviser" is another intermediary. At the request of the issuer, a confirmer, or another adviser, an adviser either notifies or requests another adviser to notify the beneficiary that the letter of credit has been issued, confirmed, or amended.[45] An adviser per se is not authorized to give value under a letter of credit and is not a nominated person.[46] But, an adviser also can be a nominated person or a confirmer.[47]

C. The Other Regimes: General Definitions

The UCP 600 term for "letter of credit" is "[c]redit [which is] any arrangement, however named or described, that is irrevocable and thereby constitutes a definite undertaking of the issuing bank to honor a complying presentation."[48] UCP 600 frequently uses terminology consistent with that of Article 5.[49] But, the roles of adviser, confirmer, issuer, and nominated person, are restricted to "banks,"[50] time is measured in "banking days,"[51] and honor and its variations like "dishonor" are spelled "honour."[52]

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45. *See* U.C.C. § 5-102(a)(1) (providing definition of "adviser").

46. *See* U.C.C. § 5-102(a)(1), (11) (noting an adviser is authorized to notify; whereas a nominated person is authorized to give value). *See, e.g.*, Banco Nacional de Desarrollo v. Mellon Bank, 726 F.2d 87, 89-92 (3d Cir. 1984) (advising that bank, that was not a nominated person, had acted at its peril in paying the beneficiary before presenting documents to the issuer, which justifiably had dishonored).

47. *See, e.g.*, U.C.C. § 5-107, cmt. 3 (noting that an advisor also can be a confirmer).

48. UCP 600, *supra* note 7, art. 2. Although revocable letters of credit are traps for the unwary, unlike UCP 600, UCP 500 permitted letters of credit that clearly indicated that they were revocable. UCP 500, *supra* note 7, art. 6(a)-(c) (explaining that in the absence of a clear indication of revocability, a letter of credit "shall be deemed to be irrevocable").

49. S*ee, e.g.*, UCP 600, *supra* note 7, art. 2 (defining "applicant" and "beneficiary").

50. *See id.* art. 2 (providing definitions of advising bank, confirming bank, issuing bank & nominated bank). *But see* DRAFTING GROUP COMMENTARY UCP 600, *supra* note 7, at 17-21 (endorsing as valid under UCP 600 an ICC Banking Commission Opinion under UCP 500 that it does not violate the UCP for a corporation that is not a bank to issue a letter of credit subject to the UCP).

51. *See* UCP 600, *supra* note 7, art. 14(b) (stating that a nominated, confirming, or issuing bank has a maximum of five banking days to determine whether a presentation of documents is complying). Banking day is defined as "a day on which a bank is regularly open at the place at which an act subject to these rules is to be performed." *See id.* art. 2. The definition is intended to count only days upon which a bank is both regularly open and open to perform acts under the UCP. *See* DRAFTING GROUP COMMENTARY UCP 600, *supra* note 7, at 15 (noting that the definition of banking day includes two distinct principles).

52. *See* UCP 600, *supra* note 7, art. 2 (defining "honour").

Rule 1.01(a) states that ISP 98 applies to performance, financial, and direct pay standbys without defining standby.[53] However, Rule 1.06 describes standbys as being irrevocable, independent, documentary, and binding undertakings,[54] and elaborates the significance of these characteristics.[55] ISP 98 usually follows the Article 5 approach. Advisers, confirmers, issuers, and nominated persons are not restricted to banks,[56] and time is measured in "business" as well as "banking days."[57] But, honor and its derivatives are spelled "honour" and adviser is spelled "advisor."[58]

III. THE NATURE OF THE ISSUER'S AND A CONFIRMER'S DEFINITE UNDERTAKING

A. Article 5

The issuer and a confirmer typically commit to honor their definite and irrevocable undertakings by paying the beneficiary upon the timely presentation of the required documents.[59] The time at which payment is due can vary. After determining that the documents presented are conforming, the most common alternatives are: prompt payment, which is referred to as payment at "sight;"[60] accepting a time draft drawn by the beneficiary,[61] followed by payment of the time draft upon its maturity;

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53. *See* OFFICIAL COMMENTARY ISP 98, *supra* note 8, rule 1.01(a); *see also id.* rule 1.01, cmt. 3 (stating that standby letter of credit is not defined).

54. *See id.* rule 1.06(a).

55. *See id.* rule 1.06(b)-(e). In order to simplify the drafting of standbys, Rule 1.06(a) adds that a standby need not describe the general characteristics delineated in Rule. 1.06. *See generally id.* rule 1.06(a), cmt. 2.

56. *See id.* rule 1.09(a) (defining "confirmer"); rule 2.01(a) (defining "issuer"); rule 2.04 (defining "nominated person"); rule 2.05 (defining "advisor"). ISP 98 also refers to "applicants" and "beneficiaries." *See* OFFICIAL COMMENTARY ISP 98, *supra* note 8, rule 1.09(a).

57. *See id.* rule 1.09(a) (defining both "business day" and "banking day"); rule 1.09, cmt. 5(a) (stating that measurement of time generally turns upon either "business days" or "banking days").

58. *See id.*; *see also* rule 1.04(iii) (noting ISP 98 ordinarily is incorporated into an agreement by an "advisor"). Unlike Article 5 and UCP 600, ISP 98 treats an advisor as a nominated person. *See id.* rule 2.04(a) ("[a] standby may nominate a person to advise.").

59. *See* U.C.C. § 5-102(a)(8) (defining "honor" as consisting of one of three types of payment unless a letter of credit provides otherwise). A confirmer has the same obligations as an issuer. *See* U.C.C. § 5-107, cmt. 1 ("[A] confirmer has the obligations [of an issuer] identified in § 5-108.").

60. An issuer has a reasonable time after presentation to examine the presented documents, but not beyond the end of the seventh business day after the day of their receipt. *See* U.C.C. § 5-108(b)(1).

61. *See infra* note 63 and accompanying text (discussing the concept of a time draft).

and incurring a deferred payment obligation, followed by the payment of the deferred obligation upon its maturity.[62] The latter two undertakings involve delayed payment. They differ in the way in which the issuer's and a confirmer's executory obligation is evidenced. A typical time draft is a written order signed by the beneficiary for the issuer or a confirmer to pay a certain number of days after a designated date, e.g., pay 30 days after sight,[63] that is separate from the letter of credit. Acceptance consists of the issuer's or a confirmer's signing the time draft,[64] which may or may not be a negotiable instrument,[65] and thereby becoming obligated to pay it.[66] A deferred payment obligation is contained within a letter of credit itself, e.g., payable 180 days after the issuer or a confirmer acknowledges that conforming documents have been presented.[67] Both

62. *See* U.C.C. § 5-102(a) (8) ("Unless the letter of credit otherwise provides, 'honor' occurs: (i) upon payment; (ii) if the letter of credit provides for acceptance, upon acceptance of a draft, and, at maturity, its payment; or (iii) if the letter of credit provides for incurring a deferred obligation upon incurring the obligation, and, at maturity, its performance."); *see generally*, DOLAN TREATISE, *supra* note 12, ¶ 1.02[1], [2], [6] (discussing payment, acceptance, and deferred payment letters of credit and observing that payment credits also are called sight credits).

63. *See* Supreme Merchandise Co. v. Chemical Bank, 503 N.Y.S.2d 9, 10 (App. Div. 1st Dept. 1986), *aff'd on other grounds*, 514 N.E.2d 1358 (1987) (involving drafts payable 30 days after sight). *See* discussion and accompanying text, *supra* note 13 (discussing drafts generally).

64. *See* U.C.C. § 3-409(a) (noting that "acceptance" is the drawee's signed agreement to pay a draft as presented and must be written on the draft but may consist of the drawee's signature alone). Under the English Bill of Exchange Act and its derivatives "acceptance" of a bill of exchange has a similar definition. *See* Bank of China v. Jian Sing Bank, HCCL 82/1999 [2000] H.K. C.F.I., ¶ 32, *available at* http://legalref.-judiciary.gov.hk/lrs/common/ju/judgment.jsp (last visited Nov. 18, 2008) (holding that the Hong Kong Bills of Exchange Ordinance requires acceptance of a bill of exchange to be written on the bill of exchange and signed by the drawee). However, on the facts, Jian Sing Bank had been estopped to deny that the bill had been signed by the drawee by the two messages that it had sent to the Bank of China stating that the bill had been accepted and that the Bank of China would be covered upon maturity. *See id.* at ¶¶ 33-37. Thus, Jian Sing Bank could not deny that it had induced the Bank of China to purchase the bill and documents. *See id.*

65. For a time draft to be a negotiable instrument it must comply with the Article 3 negotiable form requirements and not contain a conspicuous statement, however expressed, to the effect that the time draft is "not negotiable" or "not an instrument governed by U.C.C. Article 3." *See* U.C.C. §§ 3-104(a), (d). In letter of credit transactions, drafts can be in nonnegotiable form. *See* U.C.C. § 5-102, cmt. 11 (stating that an Article 5 draft can be a nonnegotiable instrument).

66. *See* U.C.C. § 3-413(a) (explaining that acceptance, which can consist of a signature upon a draft, obligates the acceptor to pay the draft).

67. *See* S. Ocean Shipbuilding Co. v. Deutsche Bank, [1993] 3 S.L.R. 686, 689 (Sing. H.C. 1993) (involving the letter of credit providing in part "[a]vailable with us for payment at 45 days after presentation of documents to us").

letters of credit involving an accepted time draft and letters of credit involving a deferred payment obligation reflect the extension of credit by the beneficiary to the applicant in the underlying transaction. Letters of credit providing for delayed payment enable the applicant to check for fraud by inspecting the goods before payment is due to the beneficiary.[68] However, under Article 5, a person that has given value, in good faith, without notice of fraud or forgery for an accepted time draft or an acknowledged deferred payment obligation of the issuer or a nominated person is immune from remedies for letter-of-credit fraud,[69] which limits the protection from fraud that the applicant otherwise would derive from the delayed payment obligation.

A well-drafted letter of credit has an expiration date and is not open-ended.[70] If there is no provision determining duration, Article 5 provides that the letter of credit expires one year after its stated date of issue; or, if there is no stated date of issue, one year after the actual date of issue.[71] A letter of credit that states it is "perpetual" is deemed to expire five years after the stated date of issue; or, if there is no stated date of issue, five years after the actual date of issue.[72]

Timely presentment consists of the beneficiary's presentation of conforming required documents at a place designated for presentation prior to expiration of the letter of credit and any earlier deadline for the

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68. *Cf.* John F. Dolan, *Discounting Deferred Payment Obligations*, 11 No. 4 DC INSIGHT 8 (Oct./Dec. 2005) (noting a deferred payment credit makes payment due after delivery and enables the issuer to determine whether there was fraud in the underlying transaction prior to payment).

69. *See* U.C.C. §§ 5-109(a) (1) (iii), (iv) (explaining that an issuer or a confirmer must honor a presentation by these persons notwithstanding letter-of-credit fraud).

70. *See* U.C.C. § 5-106, cmt. 4 ("[A]ll letters of credit should specify the date on which the issuer's engagement expires . . . .").

71. *See* U.C.C. § 5-106(c) (imposing one-year expiration date if none is stated or otherwise provided).

72. *See* U.C.C. § 5-106(d) (imposing five-year expiration date upon letters of credit that are perpetual). This is a nonvariable provision. *See* U.C.C. § 5-103(c) (listing U.C.C. § 5-106(d) as nonvariable). The provision literally applies only to letters of credit that "state" that they are perpetual. *See id.* Golden West Ref. Co. v. Suntrust Bank, 61 UCC Rep. Serv. 2d 1011 (C.D. Cal 2006), *aff'd*, 538 F.3d 1233 6-8 (9th Cir. 2008), construed the provision literally and held it to be inapplicable to a letter of credit with a one-year expiration date that nevertheless renewed automatically for additional one-year periods unless the beneficiary had given written notice of an election to terminate. *Id.* at 1020-22. Because the policy of the perpetual letter of credit ban is to protect issuers from open-ended obligations, a policy-oriented court would have converted the duration of the letter of credit in the *Golden West* case to five years. *See* James G. Barnes & James E. Byrne, *Letters of Credit*, 62 BUS. LAW. 1607, 1608-09 (2007) (stressing that the unvariable ban upon perpetual letters of credit should apply to more than letters of credit that use the word "perpetual," including letters of credit that make expiration dependent upon action by the beneficiary).

presentation of shipping documents.[73] It is immaterial that the issuer or a confirmer will require additional time to examine the presentation.[74]

The Independence Principle is a fundamental of letter-of-credit law. As expressed in Article 5, the Independence Principle, which cannot be varied by agreement,[75] severs the beneficiary's and a nominated person's entitlement to payment by the issuer or a confirmer from underlying relationships between the beneficiary, the nominated person, the issuer, the confirmer, and the applicant.[76] The obligation of the issuer and a confirmer to the beneficiary and to a nominated person is independent of the performance or the nonperformance of any contract or arrangement underlying the letter of credit, including the reimbursement agreement between the applicant and the issuer.[77] The beneficiary's or a nominated person's entitlement to payment depends upon the timely presentation of required documents that appear "on . . . [their] face strictly to comply with the terms and conditions of the letter of credit" according to the "standard practice of financial institutions that regularly issue letters of credit."[78]

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73. UCP 600, for example, requires that original transport documents, *e.g.*, original bills of lading, must be presented not later than 21 calendar days after the date of shipment, and, in any event, not later than the expiry date of the letter of credit. *See* UCP 600, *supra* note 7, art. 14(c) (stating that original transport documents must be presented within 21 calendar days after the date of shipment and prior to expiration of the letter of credit). Twenty-one calendar days is a default rule. If it is inappropriate, the parties should include a different deadline in the letter of credit. *See* DRAFTING GROUP COMMENTARY UCP 600, *supra* note 7, at 63 (noting that the deadline for presenting original transport documents should reflect the requirements of the particular transaction).

74. *See* U.C.C. § 5-108, cmt. 1 ("[T]his section applies equally to a confirmer and an issuer."); U.C.C. § 5-108, cmt. 2 ("[Pr]esentation establishes the parties' rights.").

75. *See* U.C.C. §§ 5-103(c), (d) (stating that the Independence Principle is not variable).

76. U.C.C. § 5-103, cmt. 1 (illustrating the Independence Principle by example: "That the beneficiary may have breached the underlying contract . . . is no defense for the issuer's refusal to honor").

77. *See* U.C.C. § 5-103(d). The principal Article 5 exception to the Independence Principle is material letter-of-credit fraud. *See* U.C.C. § 5-109(a) (noting that in most cases, the issuer and a confirmer, acting in good faith, can dishonor an apparently complying presentation of documents due to material letter-of-credit fraud).

78. U.C.C. §§ 5-108(a), (e). Proof of material fraud or forgery can justify good faith dishonor notwithstanding the apparent facial compliance of a documentary presentation. *See* U.C.C. § 5-109(a)(2). *But see* U.C.C. § 5-109(a)(1) (noting four categories of presenters that are entitled to honor notwithstanding proof of material fraud or forgery; *e.g.*, "a nominated person who has given value [for the required documents] in good faith and without notice of forgery or material fraud."). However, unless the applicant obtains an injunction against honor, notwithstanding the applicant's claim of material fraud or forgery, the issuer and a confirmer are free to honor a presentation in good faith, see U.C.C. § 5-109(a)(2), and are more likely to honor than to dishonor. *See* U.C.C. § 5-109,

Absent a different agreement, within a reasonable time, not to exceed seven business days after the business day of receipt of the documents, the issuer and a confirmer must determine whether documents that have been presented appear on their face to comply strictly with the terms and conditions of the letter of credit.[79] An issuer or a confirmer that fails to give to the presenter timely and complete notice of discrepancies[80] in a presentation is ordinarily precluded from asserting discrepancies of which timely notice has not been given.[81] Failure, either to honor or to give notice of dishonor, within a reasonable time is wrongful "silent dishonor."[82] Statutory strict preclusion is involved. Principles of waiver and estoppel, including the necessity of prejudicial reliance are irrelevant.[83] However, there is no preclusion with respect to the forgery of a required document, a material letter-of-credit fraud by the beneficiary upon either the issuer, a confirmer, or the applicant, or the prior expiration of the letter of credit,[84] which are not mere documentary

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cmt. 2 (noting that honor avoids the liability for wrongful dishonor that would arise if the issuer or a confirmer that dishonored could not prove material fraud or forgery in subsequent litigation).

79. *See* U.C.C. § 5-108(b) (imposing seven-business-day maximum deadline). Documents must be received at the place specified for presentation to activate the statutory deadline. *See* U.C.C. § 5-108, cmt. 2 (noting documents are considered received only at the place specified for presentation).

80. *See* discussion and accompanying text, *supra* note 37 (defining a presenter as a person presenting the required documents on its own behalf or on behalf of another).

81. U.C.C. § 5-108(c) (noting that the issuer or a confirmer is precluded from asserting most discrepancies if no timely notice was given and most discrepancies omitted from timely notice that was given). Discrepancies typically involve the presented documents, but others are possible. For example, the time and place of presentation must be complied with strictly. *See* U.C.C. § 5-108, cmt. 1 (noting that the entire presentation must appear strictly to comply). On the other hand, failure to give prompt notice to the presenter, whether the required documents will be held at the presenter's disposal or returned, which also is required, does not create preclusion. *See* U.C.C. §§ 5-108(b), (c), (h) (stating that "an issuer that has dishonored a presentation shall" advise the presenter whether the documents will be held at the disposal of the presenter or returned but failure to give this notice does not give rise to preclusion). However, an issuer's failure to acknowledge the presenter's right to dishonored documents with significant value could constitute conversion of the documents under supplementary principles of tort law. *See* Amwest Surety Co. v. Concord Bank, 248 F. Supp. 2d 867, 881-83 (E.D. Mo. 2003) (granting summary judgment to the beneficiary, ruling that the issuer had converted a sight draft and accompanying written certification by retaining the documents without notifying the beneficiary that they either would be returned or held for it).

82. *See* U.C.C. § 5-108, cmt. 2 ("[F]ailure of the issuer to act within the time permitted" is "silent dishonor.").

83. *See* U.C.C. § 5-108, cmt. 3 (emphasizing that statutory preclusion is not dependent upon principles of waiver and estoppel).

84. *See* U.C.C. §§ 5-108(c), (d) (providing that failure to give timely notice of "fraud, forgery or expiration" does not preclude the issuer with respect to these defenses); *see*

discrepancies. A nominated person that has acted upon his/her nomination is not subject to the Article 5 deadline for the examination of presented documents, the Article 5 obligation to give timely and complete notice of documentary discrepancies, or Article 5 preclusion.[85] On the other hand, having acted upon his/her nomination, a nominated person seeking reimbursement [86] is a presenter entitled to the benefit of the Article 5 deadline for the examination of presented documents, the Article 5 obligation to give timely and complete notice of discrepancies, and the Article 5 preclusion to which the issuer and a confirmer are subject.[87]

The principal exception to the Independence Principle is material letter-of-credit fraud, which may or may not involve forgery.[88] This narrow exception requires proof that the "beneficiary has no colorable right to expect honor and . . . there is no basis in fact to support such a right to honor."[89] Material fraud need not involve required documents,[90]

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also U.C.C. § 5-108, cmt. 3 (explaining untimely notice of late presentation is not preclusive). Material fraud by the beneficiary requires that the beneficiary have no colorable right to expect honor and no basis in fact to support a right to honor, a test that is derived from decisions under the 1962 text of Article 5. *See* U.C.C. § 5-109, cmt. 1 (citing cases decided under 1962 Article 5).

85. *See* U.C.C. § 5-108, cmt. 6 (stating that "[t]he section does not impose any duties on a person other than the issuer or a confirmer").

86. The issuer's and a confirmer's payment to a nominated person that had negotiated the required documents is denominated reimbursement. *See* U.C.C. §§ 5-102(a)(8), (11) (omitting the issuer's obligation to reimburse a nominated person that has negotiated from the definition of honor). Nevertheless, the right to reimbursement is comparable to the right to honor. *See* U.C.C. § 5-108, cmt. 5 (noting the issuer has the same obligations with respect to presentment for reimbursement and presentment for honor).

87. *See* U.C.C. § 5-108(b)(3) (requiring that notice of discrepancies be given to the presenter); U.C.C. § 5-108(b)(3), cmt. 5 ("[N]ominated persons can . . . be presenters and, when so, are entitled to the notice of discrepancies provided in subsection (b).").

88. See U.C.C. § 5-109(a) (explaining that the issuer, acting in good faith, ordinarily either may honor or dishonor a presentation alleged to involve material fraud or forgery). In two other instances, the Independence Principle is qualified to allow consideration of an underlying transaction for a specific purpose: (1) breach of a statutory warranty by a beneficiary that has obtained honor, *see* U.C.C. § 5-110(2) subrogation of an unreimbursed issuer that has honored a presentation, an applicant that has reimbursed the issuer, and an unreimbursed nominated person that has given value under a letter of credit to the rights of another to the same extent as a secondary obligor would be subrogated, *see* U.C.C. § 5-117.

89. *See id.* U.C.C. § 5-109, cmt. 1. *Compare* Intrinsic Values Corp. v. Supintendencia de Administracion Tributaria, 806 So. 2d 616, 618 (Fla. App. 2002) (noting beneficiary that had been aware that the underlying contract had been cancelled prior to presentation had no basis in fact to support a right to honor), *with* Sava Gumarska In Kemijska Industria v. Advanced Polymer Sciences, Inc., 128 S.W.3d 304, 321-23 (Tex. App. 2004) (noting breach of the underlying contract by the beneficiary and a failure by the beneficiary to disclose information per se are not material letter-of-credit fraud).

nor is the involvement of a required document conclusive evidence of material fraud. In order to be material, either the fraudulent aspect of a required document with intrinsic value must be important to a purchaser of the document or the fraudulent aspect of a required document must be important to the parties in the underlying transaction.[91] An Official Comment, for example, states that a required invoice overstating the number of barrels in 1,000-barrel shipment of salad oil by two would be immaterial; whereas a required invoice overstating the number of barrels by 995 would be highly material.[92]

Material fraud justifies good faith dishonor of a presentation by the issuer or a confirmer notwithstanding the apparent facial compliance of the required documents.[93] However, unless the applicant obtains an injunction against honor and reimbursement,[94] notwithstanding the

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90. *See, e.g.*, Mid-America Tire, Inc. v. PTZ Trading Ltd., 768 N.E.2d 619, 639, 641-42 (Ohio 2002) (noting beneficiary induced applicant to obtain issue of letter of credit with respect to winter tires that could not be imported legally by materially false representations with respect to both importability and the availability of more lucrative summer tires); James G. Barnes & James E. Byrne, *Letters of Credit: 2001 Cases*, 7 BUS. LAW. 1725, 1730 (2002) (positing that fraud need not be in the documents presented).

91. *See* U.C.C. § 5-109, cmt. 1 ("[T]he fraudulent aspect of a document [must] be material to a purchaser of that document or . . . the fraudulent act [must] be significant to the participants in the underlying transaction.").

92. *See id.*

93. *See* U.C.C. § 5-109(a)(2) (acting in good faith, the issuer can dishonor an apparently strictly complying presentation of documents if a required document is forged or materially fraudulent or honor otherwise would facilitate a material fraud by the beneficiary). Because the context does not require otherwise, the references to "issuer" in Section 5-109 includes a confirmer. *See* U.C.C. § 5-107, cmt. 1 (unless the context requires otherwise, a reference to the "issuer" includes a confirmer). *But see* U.C.C. § 5-109(a)(1) (noting four categories of presenters are entitled to honor notwithstanding proof of material fraud or forgery by the beneficiary; for example, "a nominated person who has given value [for the documents] in good faith and without notice of the forgery or material fraud").

94. An injunction against honor and reimbursement is subject to the following statutory safeguards: (1) there must be no prohibition against injunctive relief in the law applicable to a draft accepted by the issuer or a confirmer or a deferred obligation incurred by the issuer or a confirmer; (2) the applicant must provide adequate protection against loss to an adversely affected beneficiary, issuer, or nominated person; (3) the applicant must satisfy the general state prerequisites for injunctive relief, like the inadequacy of the remedy at law; and (4) the court must find that the applicant is more likely than not to be able to prove material fraud or forgery and that the person demanding honor is not protected from injunctive relief by Article 5. *See* U.C.C. §§ 5-109(a)(1), (b). For discussion of the persons protected from injunctive relief for material fraud, see discussion and accompanying text, *infra* notes 97-110. Intrinsic Values Corp. v. Superintendencia de Administracion Tributaria, 806 So. 2d 616 (Fla. App. 2002) involved an applicant's injunction against honor by two confirmers due to material fraud. A more limited form of injunctive relief is also possible. An applicant, for example, could

applicant's claim of material fraud, the issuer and a confirmer, acting in good faith, are free to honor or to reimburse a presentation,[95] and are more likely to honor and to reimburse than to dishonor.[96]

Article 5 immunizes four categories of persons from both a defense and an injunction based upon material fraud. The protected classes are:

> (1) nominated persons that have given value in good faith and without notice of material fraud; (2) confirmers that have honored their confirmations in good faith; (3) holders in due course[97] of accepted time drafts drawn under letters of credit that had acquired the drafts after their acceptance by the issuer or a nominated person; and (4) assignees of the issuer's or a nominated person's deferred payment obligation that had obtained their assignments for value and without notice of material fraud after the deferred payment obligation had been incurred.[98]

The first two categories of protected persons involve nominated persons.[99] The other two categories require that a protected assignee of a deferred payment obligation and a protected holder in due course of an accepted time draft have acquired rights created by either the issuer or a nominated person, but the protected assignee or holder in due course

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enjoin a nominated negotiating bank from negotiating and acquiring immunity from remedies for material fraud. *See* U.C.C. § 5-109(b) (stating the applicant can enjoin "other persons" in addition to the issuer); Jim Barnes, *UCP 600 and Bank Responsibility for Fraud*, 13 NO. 1 DC INSIGHT 5, 7 (Jan./Mar. 2007) (stating this type of injunction would deprive a fraudulent beneficiary of funds without prejudicing the nominated negotiating bank, even if the negotiating bank had an executory obligation to make an advance for the documents).

95. *See* U.C.C. § 5-109(a)(2) (noting, in addition to the four categories of presenters entitled to honor, acting in good faith, the issuer and a confirmer can honor other apparently strictly complying presentations notwithstanding the applicant's claim of material fraud or forgery).

96. *See* U.C.C. § 5-109, cmt. 2 (noting that honor avoids the liability for wrongful dishonor that would arise if the issuer dishonored but could not prove material fraud in subsequent litigation).

97. The holder in due course of an Article 3 negotiable instrument is a privileged transferee that takes free of many claims and defenses. *See* U.C.C. § 3-305(b) (distinguishing defenses to which a holder in due course is and is not subject).

98. *See* U.C.C. § 5-109(a)(1) (listing the four categories).

99. *See* U.C.C. §§ 5-109(a)(1)(i), (ii) (mandating that clause (i) is expressly limited to nominated persons and clause (ii) is limited to confirmers, which must be nominated persons). *See* U.C.C. § 5-102(a)(4) ("'Confirmer' means a nominated person . . . .").

need not be a nominated person.[100] Otherwise, even the holder in due course of an unaccepted draft drawn by the beneficiary under the letter of credit acts at his or her own risk, stands in the shoes of the beneficiary, and is subject to remedies for material letter-of-credit fraud.[101]

There is an important distinction between the immunity of confirmers and the other immunities. A confirmer that honors its confirmation in good faith is immune even though the confirmer previously had been notified of alleged material fraud;[102] whereas the other three immunities are contingent upon the good faith acquisition of rights without notice of material fraud.[103] Their broader immunity is designed to encourage honor by confirmers that have been notified by applicants of alleged fraud.[104]

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100. *See* U.C.C. §§ 5-109(a)(1)(iii)-(iv); *see also* James G. Barnes & James E. Byrne, *Letters of Credit: 2004 Cases*, 60 BUS. LAW 1699, 1706 (2005) (stating an adviser that had not been nominated to negotiate would not qualify under revised Article 5 for protection from letter-of-credit fraud upon the basis of holder in due course status with respect to the beneficiary's unaccepted draft).

101. *See, e.g.*, Credit Agricole Indosuez v. Banque Nationale, [2001] 2 S.L.R. 1, at 5, 13-14 (Sing. C.A. 2001) (holding that the credit was not a negotiation credit and the advising and confirming bank that had purchased the required documents from the beneficiary was subject to a letter-of-credit fraud defense); *see* JAMES J. WHITE & ROBERT S. SUMMERS, UNIFORM COMMERCIAL CODE 193 (Practitioner's Treatise 4th ed. West 1995) [hereinafter WHITE & SUMMERS TREATISE] (stating that a holder in due course of the beneficiary's unaccepted draft under a straight credit stands in the shoes of the beneficiary); *see also* UCC § 5-116(d) (stating that Article 5 governs conflicting provisions in Article 3 with respect to the rights and immunities of a holder in due course of an Article 3 negotiable instrument). *See* U.C.C. § 3-305(a), (b) (listing Article 3 rights and immunities of a holder in due course).

102. *Compare* U.C.C. § 5-109(a)(1)(i) (noting that for immunity to exist, a nominated person must have given value in good faith and without notice of forgery or material fraud), *with* U.C.C. § 5-109(a)(1)(ii) (noting that for immunity to exist, a confirmer must have honored its confirmation in good faith). Although the Article 5 immunity provision for holders in due course does not explicitly refer to acquiring a negotiable instrument in good faith and without notice of material fraud, the Article 3 prerequisites for a holder in due course status require this. *See* U.C.C. § 3-302(a)(2) (requiring a holder in due course to acquire a negotiable instrument in good faith and without notice of a claim or a defense).

103. *See* U.C.C. §§ 5-109(a)(1)(i), (iii), (iv) (explaining that for immunity to exist a nominated person and an assignee of a deferred payment obligation of the issuer or a nominated person must have "given value without notice of forgery or material fraud" and a transferee of a time draft (that had been accepted by the issuer or a nominated person) must be a holder in due course of the time draft). Article 3 requires that a holder in due course have acquired a negotiable instrument for value and without notice of fraud by a party to the instrument. *See* discussion and accompanying text, *supra* note 102.

104. *See* James G. Barnes, *A US View: US Codified Law is Superior to English Judge-Made Law On the Fraud Exception to the Independence of Letters of Credit*, 6 NO. 3 DC INSIGHT 7, 8 (July/Sept. 2000) ("[P]utting banks at risk for honouring after receipt of notice of fraud will induce dishonour.").

For purposes of the immunity provisions, "good faith" means honesty in fact in the conduct or the transaction concerned;[105] "without notice" means without reason to know of material letter-of-credit fraud from the facts and circumstances known to a person;[106] and "value"[107] includes the payment or securing of an antecedent debt owed to anyone,[108] provisional credit that has been withdrawn or applied, provisional credit that is available for withdrawal as a matter of right, and an advance.[109] However, an executory promise that is not embodied either in a negotiable instrument or in an irrevocable promise to a third party is not value.[110]

B. The Other Regimes

Following the determination that the presented documents are complying, like Article 5, UCP 600 defines honour as "pay[ing] at sight if the credit is available by sight payment," "accept[ing a time draft] drawn by the beneficiary and pay[ing] at maturity if the credit is available by acceptance," and "incur[ring] a deferred payment [obligation] and pay[ing] at maturity if the credit is available by deferred

105. *See* U.C.C. § 5-102(a)(7). Article 5 rejects the general U.C.C. expansion of the concept of good faith to include "observance of reasonable commercial standards of fair dealing" in order to provide greater certainty with respect to the existence or nonexistence of good faith. *See* U.C.C. § 5-102(a)(7), cmt. 3 (noting that Article 5 has a narrower definition of good faith than other U.C.C. Articles).

106. *See* U.C.C. §1-202(a)(3) (stating that a person has notice of a fact if the person has reason to know that the fact exists from the other known facts and circumstances).

107. *See* U.C.C. § 5-102(b) ("Definitions in other Articles applying to . . . [Article 5] and the sections in which they appear are . . . 'Value' Sections 3-303, 4-211.").

108. *See* U.C.C. § 3-303(a)(3) (stating that issue or transfer of a negotiable instrument as payment of or as security for an antecedent claim against anyone is value, whether or not the claim is due).

109. *See* U.C.C. § 4-210(a), 2B Part 1 U.L.A. 63 (Master ed. 2002) (stating that a collecting bank has a statutory security interest in an item being collected, accompanying documents, and proceeds to the extent that provisional credit for the item has been withdrawn or applied, provisional credit for the item is available for withdrawal as of right, whether or not withdrawn, or an advance has been made on or against the item). [hereinafter cited as U.C.C. art. 4 Section Number]. Section 4-211 provides that a collecting bank has given value to the extent that it has a statutory security interest in an item. *See* U.C.C. § 4-211; U.C.C. amended §§ 4-101 to 4-504.

110. *See* U.C.C. §§ 3-303(a) (1), (4), (5) (stating that a promise that is not embodied in a negotiable instrument or an irrevocable promise to a third party is value only to the extent that it has been performed). When the exceptions do not apply, a promisor that learns of fraud before performing its promise can protect itself by not performing. *See* U.C.C. § 3-303, cmt. 2 (stating that the maker of an executory promise can avoid out-of-pocket loss by not performing).

payment."[111] The issuing bank's and a confirming bank's payment of its obligation to a nominated negotiating bank that has negotiated the required documents and forwarded them is described as reimbursement rather than honour.[112] Nevertheless, a nominated negotiating bank that has negotiated and forwarded the required documents for reimbursement is a presenter.[113]

ISP 98 only appears to conceptualize honour more broadly. Unless a standby provides otherwise, the issuer and a confirmer[114] honour by paying the amount demanded at sight.[115] Alternative provisions authorize honour by: the timely acceptance of a time draft drawn by the beneficiary and the payment of the draft upon its presentation on or after its maturity, the timely incurring of a deferred payment obligation and the payment of that obligation on or after its maturity, and the timely negotiation of a draft by paying the amount demanded at sight.[116] Official Comment 8 observes that the issuer's honour by negotiation typically involves a draft

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111. *See* UCP 600, *supra* note 7, art. 2 (explaining that the definition refers to a bill of exchange as well as a draft). *See* discussion and accompanying text, *supra* notes 59-67 (explaining the Article 5 definition).

112. *See* UCP 600, *supra* note 7, art. 2 (omitting reimbursement of a nominated person in definition of honour), art. 7(c) (stating that the issuing bank's obligation to reimburse a nominated bank that has negotiated the required documents and forwarded them to the issuing bank is independent of the issuing bank's obligation to the beneficiary), art. 8(c) (stating that a confirming bank's obligation to reimburse a nominated bank that has negotiated the required documents and forwarded them to the confirming bank is independent of the confirming bank's obligation to the beneficiary). Article 5 also characterizes payment to a nominated person that has negotiated as reimbursement. Nevertheless, a right to reimbursement and a right to honour are essentially the same. *See* discussion and accompanying text, *supra* note 86.

113. *See* UCP 600, *supra* note 7, art. 2 (stating that a presenter is the party that makes a presentation of documents), 15(c) (after a nominated bank has honoured or negotiated, it must forward the documents to the issuing bank or a confirming bank). *See also* JAMES E. BYRNE, THE COMPARISON OF UCP600 & UCP500 43 cmt. 7 (Inst. Int'l Banking L. & Pract. 2007) [hereinafter COMPARISON OF UCP600 & UCP500]. Byrne states:

> There is no distinction in UCP 600 . . . between a presentation by a nominated bank and one by a bank that is not nominated A correspondent bank that is not nominated makes a presentation on behalf of the beneficiary whereas a nominated bank that acts pursuant to its own nomination makes a presentation on its own behalf as well.

Id.

114. *See* OFFICIAL COMMENTARY ISP 98, *supra* note 8, rule 1.11(c)(i) (stating that, unless the context otherwise requires, "issuer" includes a "confirmer").

115. *See id.* rule 2.01(b) (explaining that, absent a different standby provision, honour is payment of the amount demanded at sight).

116. *See id.* rule 2.01(b)(i)-(iii) (elaborating permissible methods of honour that do not involve payment at sight upon demand).

designating the applicant as drawee.[117] This type of honour by negotiation can not occur under the Official Text of UCP 600, which prohibits making a credit available by a draft drawn upon the applicant.[118] ISP 98 recognizes the issuer's and the confirmer's obligation to reimburse a nominated person that has given value for complying documents,[119] and treats a nominated person seeking reimbursement as a presenter.[120]

Under UCP 600, an issuing bank, a confirming bank, and a nominated negotiating bank that has elected to negotiate[121] have a maximum of five banking days following the banking day of presentation to determine whether the presentation is complying. The occurrence on or after the banking day of presentation of the expiry date or the last date for the presentation of shipping documents does not affect the deadline.[122] The test for compliance is whether the documents

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117. *See id.* rule 2.01, cmt 8 ("Typically, this situation arises when the standby requires that the draft be drawn upon the applicant.").

118. *See* UCP 600, *supra* note 7, art. 6(c) (stating that a credit must not be issued available by a draft drawn on the applicant). The rationale is that a letter of credit that conditions availability upon drafts drawn upon the applicant would not assure payment if the applicant was dissatisfied with the underlying transaction. *See* DRAFTING GROUP COMMENTARY UCP 600, *supra* note 7, at 34 (stating that a documentary credit available by a draft drawn upon the applicant can bring the applicant into the settlement process). However, Article 6(c) does not preclude a draft drawn upon the applicant to be one of the required documents. *See id.* (stating that a draft drawn upon the applicant can be a required document). A letter of credit that provided for drafts drawn upon the applicant would cancel the UCP 600 prohibition. *See* COMPARISON OF UCP600 & UCP500, *supra* note 113, cmt. 9, at 81 (stating that a provision in a letter of credit requiring a draft to be drawn upon the applicant would vary UCP 600). UCP 600 also excludes a nominated bank's purchase of drafts drawn upon the nominated bank from its concept of negotiation. *See* UPC 600, *supra* note 7, art. 2 (stating that negotiation involves a nominated bank's purchase of drafts not drawn upon the nominated bank).

119. *See* OFFICIAL COMMENTARY ISP 98, *supra* note 8, rule 8.01(a)(ii) (stating that an issuer must reimburse a person nominated to give value that has done so in accordance with ISP 98).

120. *See id.* rule 1.09(a) ("[P]resenter is a person who makes a presentation as or on behalf of a beneficiary or nominated person.").

121. *See* James E. Byrne, *Negotiation in Letter of Credit Practice and Law: The Evolution of the Doctrine*, 42 TEX. INT'L L.J. 561, 569 n.22 (2007) (stating that a nominated bank is not bound by any time limits until it elects to act upon the nomination). UCP 600 does not impose meaningful time limits upon nominated negotiating banks that have elected to negotiate. *See infra* notes 157-158 and accompanying text. Like Article 5, UCP 600 does not require nominated banks that are not confirmers to act upon their nominations. *See* UCP 600, *supra* note 7, art. 12(a) (stating that unless it is a confirmer or expressly has agreed to do so, a nominated bank need not act upon its nomination).

122. *See* UCP 600, *supra* note 7, art. 14(b) (stating that the issuing bank, a confirming bank, and a nominated bank shall have a maximum of five banking days to determine

presented on their face appear to be in accord with the terms and conditions of the credit, UCP 600, and international standard banking practice.[123] If the presentation is complying, the issuing bank must honour without retaining a right of recourse against the presenter.[124] In addition, a confirming bank either must honour or negotiate, whichever it has been nominated to do, and forward the documents to the issuing bank.[125] If a presentation is complying, a nominated negotiating bank that has acted upon its nomination must forward the documents to the issuing bank or to a confirming bank.[126] If the issuing bank, a confirming bank, or a nominated bank, acting upon its nomination, decides to refuse to honour or to refuse to negotiate, it must give the presenter a single notice stating that it is refusing to honour or to negotiate, and identify all the discrepancies, by telecommunication if possible, otherwise by other expeditious means, no later than the close of the fifth banking day after the banking day of presentation.[127] Notwithstanding the deletion by UCP

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whether 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). The mere receipt of documents by a nominated negotiating bank that has neither agreed to negotiate nor acted on its nomination does not obligate the nominated bank to examine the documents. DRAFTING GROUP COMMENTARY UCP 600, *supra* note 7, at 62 (stating that a nominated bank that neither has agreed to negotiate nor acted upon its nomination is not obligated to comply with art. 14 on examination of documents). UCP 500 had allowed a maximum of seven banking days. *See* UCP 500, *supra* note 7, art. 13(b) (providing that the issuing bank, a confirming bank, and a nominated bank shall have a reasonable time, not to exceed seven banking days, following the banking day of receipt of the documents to determine whether to take them up or to refuse them).

123. *See* UCP 600, *supra* note 7, art. 2 (explaining that an issuing bank, a confirming bank, and a nominated bank must determine, on the basis of the documents alone, whether or not the documents on their face constitute a complying presentation); art. 14(a) (defining a "complying presentation" as a presentation in accordance with the terms and conditions of the credit, these rules, and international standard banking practice).

124. *See* UCP 600, *supra* note 7, art. 15(a) (explaining that an issuing bank must honour a complying presentation). Retaining a right of recourse against the presenter would be inconsistent with the issuing bank's obligation to honour. *See* COMPARISON OF UCP600 & UCP500, *supra* note 113, cmt. 9(a), at 81-82 (noting that an issuing bank is obligated to honour conforming documents without recourse).

125. *See* UCP 600, *supra* note 7, art. 15(b) (explaining that a confirming bank must honour or negotiate and forward the documents to the issuing bank). A confirming bank that negotiates must do so without recourse to the presenter. *See* UCP 600, *supra* note 7, art. 8(a)(ii) (stating that a confirming bank must negotiate without recourse). Retaining recourse to the presenter in the event that the issuing bank dishonors is inconsistent with the confirming bank's obligation to negotiate.

126. *See* UCP 600, *supra* note 7, art. 15(c) (explaining that a nominated bank must negotiate and forward the documents to the issuing bank or to a confirming bank).

127. *See* UCP 600, *supra* note 7, art. 16(c)-(d) (explaining that a single notice of refusal to honour or notice of refusal to negotiate, identifying each discrepancy must be

600 of the UCP 500 requirement that notice of refusal must be given "without delay," the reference to "no later than the close of the fifth banking day" would not protect an issuing or a confirming bank that unnecessarily waited until the fifth banking day to give notice of refusal.[128] UCP 600 also does not displace the explicit Article 5 rule that a reasonable time for examination can expire before the outside deadline.[129]

An issuing or a confirming bank that fails to give timely and complete notice to presenter of refusal to honour or refusal to negotiate is strictly precluded from claiming that the presentation had been noncomplying with respect to most discrepancies that had not been the subject of the single timely notice.[130] But, although a nominated bank that has acted upon its nomination is not subject to UCP 600 preclusion, the nominated bank is obligated by any agreements made with the beneficiary and also can be liable for prejudicially misleading the beneficiary.[131] Nevertheless, a nominated negotiating bank that negotiated is a presenter and entitled to the benefit of the UCP 600 deadline for the examination of presented documents, the UCP 600

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given by telecommunication, if possible, or by other expeditious means no later than the close of the fifth banking day following the day of presentation).

128. *See* COMPARISON OF UCP600 & UCP500, *supra* note 113, cmts. 10(d), (e), (h), at 132-33 (explaining that the five days are a safe harbor but less time could be allowed under certain circumstances; if the issuing bank had reached a decision with respect to honour in less than five banking days and had delayed giving notice of refusal without justification consequences may follow). *See id.* cmt. 15, at 149 ("Even where a bank has not deliberately delayed but has failed to act within its own standards and those of the industry in giving notice after examination without any plausible excuse, it may be wondered whether this five day period will be treated as a safe harbor . . . .").

129. *See PTZ Trading Ltd.*, 768 N.E. 2d at 636-37 (stating that, if the UCP does not contain a rule on a topic, incorporation of the UCP does not displace the Article 5 rule). *See* discussion and accompanying text, *supra* notes 79-83 (discussing the Article 5 rule).

130. *See* UCP 600, *supra* note 7, art. 16(f) (stating that an issuing or a confirming bank that fails to act in compliance with art. 16 is precluded from claiming that the documents do not constitute a complying presentation). UCP 500 had required that notice of refusal of the documents be given by telecommunication, if possible, or other expeditious means no later than the close of the seventh banking day following the day of receipt of the documents. *See* UCP 500, *supra* note 7, art. 14(d)(i) (stating that notice must be given by telecommunication, if possible, or by other expeditious means without delay no later than the close of the seventh banking day following the day of receipt of the documents). UCP strict preclusion does not require prejudicial reliance by a beneficiary upon the issuer's or a confirmer's conduct. *See* Kerr-McGee Chem. Corp. v. FDIC, 872 F.2d 971, 973-75 (11th Cir. 1989) (holding that failure to give timely notice of dishonor under UCP 400 created per se estoppel).

131. *See* UCP 600, *supra* note 7, art. 16(f), which imposes preclusion solely upon issuing and confirming banks; *see also* U.C.C. § 5-108, cmt. 6 (explaining that a nominated person can have common-law liability to the beneficiary).

obligation to give a single timely notice of discrepancies, and the UCP 600 preclusion to which the issuer and a confirmer are subject.[132]

The UCP 600 preclusion rule with respect to issuing and confirming banks applies to a failure to give the timely notice of refusal to honour or refusal to negotiate required by UCP 600 Article 16. Exceeding the deadline for the examination of presented documents under UCP 600 Article 14 is not subject to preclusion.[133] UCP 600's lack of a preclusion rule with respect to unreasonable delay in examining documents does not displace the explicit Article 5 rule precluding issuers and confirming banks that have engaged in dilatory examination.[134]

UCP 600 and ISP 98 have substantially similar tests for compliance of the documents presented,[135] requirements for an expiration date,[136]

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132. *See id.* art. 14(a) (explaining that an issuing and a confirming bank have a maximum of five banking days to examine a presentation), art. 16(c) (stating that issuing and confirming banks must give timely notice of refusal of documents to the presenter), art. 16(f) (explaining that to the extent of their noncompliance, issuing and confirming banks that have failed to act in compliance with Article 16 are precluded from claiming that the documents do not constitute a complying presentation). Article 2 defines a presenter as any bank or party that makes a presentation of documents. *See id.* art. 2 (stating that presenters include any bank or party that makes a presentation).

133. *See id.* art. 16(f) (stating that an issuing or confirming bank that fails to act in compliance with Article 16 is precluded from claiming that the documents do not constitute a complying presentation). If the preclusion rule is limited to undue delay under Article 16, the time taken in deciding to reject a presentation would be irrelevant. Undue delay would involve solely taking too long to notify the presenter after having decided to reject the documents. *See* NV Koninklijke Sphinx Gustavsberg v. Cooperatieve Centrale Raiffeisen-Boerenleenbank, HCCL 188/1997 [2004] H.K. C.F.I., ¶¶ 11-12, 38-43, *available at* http://legalref.judiciary.gov.hk/lrs/common/ju/judgment.jsp (last visited Nov. 18, 2008), *appeal allowed in part on other grounds*, CACV 161/2004 (H.K. C.A. 2005), *available at* http://legalref.judiciary.gov.hk/lrs/common/ju/-judgment.jsp (last visited Nov. 18, 2008) (noting that because the UPC 500 preclusion rule does not apply to undue delay in examining documents, the only relevant delay is between the decision to reject the documents and notification of that decision). With respect to the maximum period for examination of presented documents under UCP 600, refer to discussion, *supra* notes 121-122. Likewise, UCP 500 had divorced issuing and confirming banks' deadline for examination of documents from its preclusion rule. *See* DOLAN TREATISE, *supra* note 12, at 6-76 & 6-77 (discussing the UCP 500 "drafting glitch"). A California intermediate appellate court nevertheless ruled that the UCP 500 preclusion rule applied to an issuing bank's failure to comply with the deadline for examining presented documents. *See DBJJJ, Inc.*, 29 Cal Rptr. 3d at 912, 915-16 (stating that, if, on remand, the beneficiary proved that the issuing bank had exceeded a reasonable time in deciding to dishonor, the issuing bank would be precluded from claiming that the documents did not comply).

134. *See PTZ Trading Ltd.*, 768 N.E. 2d at 637 (stating that, if the UCP has no rule upon a topic, incorporation of the UCP does not displace the Article 5 rule). *See* discussion and accompanying text, *supra* notes 81-83 (discussing the Article 5 rule).

135. *See* UCP 600, *supra* note 7, arts. 2, 14(a) (stating in Article 14(a) that an issuing or a confirming bank must determine, on the basis of the documents alone, whether or not

expressions of the Independence Principle,[137] and exclusions of nominated persons from the preclusion to which the issuer and a confirmer are subject.[138] Both UCP 600 and ISP 98 also generally omit provisions on material letter-of-credit fraud, leaving this to other law, including Article 5.[139] On the other hand, in addition to having a seven-

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the documents on their face constitute a complying presentation; defining in Article 2 a "complying presentation" as a presentation in accordance with the terms and conditions of the credit, these rules, and international standard banking practice); OFFICIAL COMMENTARY ISP 98, *supra* note 8, rule 4.01(b) (explaining that whether a presentation appears to comply is determined by examining the presentation on its face against the terms and conditions stated in the standby as interpreted and supplemented by ISP 98, which is to be read in the context of standard standby practice).

136. *See* UCP 600, *supra* note 7, art. 6(d) (stating that a credit must state an expiry date for presentation; an expiry date for honour or negotiation also is deemed to be an expiry date for presentation); OFFICIAL COMMENTARY ISP 98, *supra* note 8, rule 9.01(stating that a standby either must contain an expiry date or permit the issuer to terminate the standby upon reasonable prior notice or payment).

137. *See* UCP 600, *supra* note 7, art. 4(a). Article 4(a) of UCP 600 states:

> A credit by its nature is a separate transaction from the sale or other contract on which it may be based. Banks are in no way concerned with or bound by such contract, even if any reference whatsoever to it is included in the credit. Consequently, the undertaking of a bank to honour, to negotiate or to fulfill any other obligation under the credit is not subject to claims or defences by the applicant resulting from its relationships with the issuing bank or the beneficiary.

Id. See also OFFICIAL COMMENTARY ISP 98, *supra* note 8, rule 1.06(c). The Official Commentary states:

> Because a standby is independent, the enforceability of an issuer's obligations under a standby does not depend on: (i) the issuer's right or ability to obtain reimbursement from the applicant; (ii) the beneficiary's right to obtain payment from the applicant; (iii) a reference in the standby to any reimbursement agreement or underlying transaction; or (iv) the issuer's knowledge of performance or breach of any reimbursement agreement or underlying transaction.

Id.

138. *Compare* UCP 600, *supra* note 7, art. 16(f) (precluding issuing and confirming banks), *with* OFFICIAL COMMENTARY ISP 98, *supra* note 8, rule 5.03(a), cmt. 8 (applying preclusion only to issuers and confirmers). ISP 98, like UCP 600, also gives nominated persons that have acted upon their nominations and presented the required documents for reimbursement by the issuer or a confirmer the benefit of the ISP 98 deadline for examination of documents, *see id.* rule 5.01(c), and the preclusion of the issuer and a confirmer from relying upon most discrepancies omitted from a timely notice of refusal. *See id.* rule 5.03, cmts. 1, 8 (noting that this rule precludes the issuer or a confirmer from subsequently asserting a discrepancy not stated in a timely notice of dishonor).

139. *See* UCP 600, *supra* note 7, art. 14(a) ("[T]he 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."), art. 34 ("A bank assumes no responsibility for the form, sufficiency, accuracy, genuineness, falsification, or legal effect of any document . . . ."); OFFICIAL COMMENTARY ISP 98,

business-day deadline for the issuer to give expeditious notice of dishonour and discrepancies,[140] ISP 98 defers to the issuer's judgment by focusing upon whether the notice given had been unreasonable. Notice that had been given within three business days after the business day of presentation is deemed to not be unreasonable and notice that had been given after the expiration of seven business days is deemed to be unreasonable.[141] Whether notice that had been given between four and seven business days after the business day of presentation is unreasonable depends upon the circumstances.[142] The ISP 98 preclusion rule applies to all failures by the issuer or a confirmer to give timely notice of refusal of the documents.[143] ISP 98 omits the separate UCP 600 deadlines for examination and giving notice of refusal.[144]

UCP 600 does not explicitly exclude material fraud, forgery, or the prior expiration of the letter of credit from its strict preclusion rule. However, UCP 600 Article 16 is captioned "Discrepant Documents" and emphasizes discrepancies in the presented documents.[145] Material fraud, forgery and the expiration of a letter of credit also are not dealt with by

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supra note 8, rule 1.05(c) ("These Rules do not define or otherwise provide for: . . . (c) defenses to honour based on fraud, abuse, or similar matters. These matters are left to applicable law."). UCP 600 has one provision that was intended to increase the immunity from material letter-of-credit fraud of a nominated bank that has acted upon its nomination. *See* discussion, *infra* notes 259-285 (discussing the *Banco Santander* exception). UCP 600 also has added express statements that an issuing and a confirming bank's obligation to reimburse a nominated bank is independent of any obligation to the beneficiary. *See* UCP 600, *supra* note 7, arts. 7(c), 8(c) (explaining that the undertaking to reimburse a nominated bank is independent of the undertaking to the beneficiary). This elaboration of the Independence Principle should enhance nominated banks' immunity from beneficiary fraud. *See* Jim Barnes, *UCP 600 and Bank Responsibility for Fraud*, 13 No. 1 DC INSIGHT 5, 6 (Jan./Mar. 2007) ("By clarifying a nominated bank's reimbursement rights, UCP 600 effectively strengthens those rights.").

140. *See* OFFICIAL COMMENTARY ISP 98, *supra* note 8, rule 5.01(a)(i) (deeming notice given beyond seven business days unreasonable).

141. *See id.* rule 5.01(a)(i). ISP 98 adopted an "unreasonable notice" test in lieu of a "reasonable notice" test in order to allow issuers the latitude permitted by standard correspondent banking practice. *See id.* rule 5.01, cmt. 4 ("This Rule reverses the formulation because it has been misunderstood as an invitation to determine what is reasonable rather than, as intended, its outer limit.").

142. *See id.* rule 5.01, cmts. 4, 6 (stating that unreasonableness should be determined by standard correspondent banking practice and the circumstances).

143. *See id.* rule 5.03(a) ("Failure to give notice . . . within the time and by the means specified in the standby or these rules precludes . . . .").

144. *Compare id.*, *with* discussion and accompanying text, *supra* notes 122, 127 (discussing the UCP 600 approach).

145. *See* UCP 600, *supra* note 7, art. 14(a) (requiring that the "documents" appear on their face to be a complying presentation); *id.* art.16(a) (explaining that an issuing and a confirming bank may refuse to honour a presentation that does not comply).

other aspects of UCP 600, which does not displace their exclusion from Article 5 preclusion.[146] ISP 98 expressly excludes only notice of expiry from preclusion.[147] But ISP 98 does not deal with material fraud and forgery,[148] and likewise does not displace their exclusion from Article 5 preclusion.[149]

C. The Effect of the Incorporation of UCP 600 or ISP 98 into a Letter of Credit Subject to Article 5

Incorporation of UCP 600 or ISP 98 into a letter of credit subject to Article 5 alters conflicting variable[150] Article 5 rules but not consistent variable Article 5 rules.[151] Explicit conflict between an incorporated rule and a variable Article 5 rule displaces the Article 5 rule. It is unnecessary for the incorporated rule expressly to state that it varies Article 5.[152] On the other hand, if incorporated rules of practice have no counterpart for a variable Article 5 rule, the Article 5 rule is not displaced.[153]

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146. *See PTZ Trading Ltd.*, 768 N.E. 2d at 634-37 (stating that UCP 500, which does not deal with material fraud, does not displace the Article 5 material fraud provisions). Boston Hides & Furs, Ltd. v. Sumitomo Bank, 870 F. Supp. 1153, 1162-64 (D. Mass. 1994) (limiting the exclusion from preclusion to latent fraud). This case was decided under the 1962 version of Article 5, which contained neither an express preclusion rule nor express exceptions from preclusion. *Id.*; *See also* ABA Task Force on the Study of Article 5, *An Examination of U.C.C. Article 5 (Letters of Credit)*, 45 BUS. LAW. 1521, 1601 (1990) ("The cases under the [1962] U.C.C. do not preclude the raising of objections in addition to those originally raised unless the beneficiary can establish the affirmative defense of waiver or estoppel . . . .").

147. *See* OFFICIAL COMMENTARY ISP 98, *supra* note 8, rule 5.04 ("Failure to give notice that a presentation had been made after the expiration date does not preclude dishonour for that reason.").

148. *See id.* rule 1.05(c) (noting that defenses to honour based upon fraud, abuse, or similar matters are left to applicable law).

149. *See* discussion and accompanying text, *supra* note 146.

150. *See* discussion and accompanying text, *supra* note 9 (discussing the Article 5 nonvariable rules and noting all other Article 5 rules are variable).

151. *See* U.C.C. § 5-116(c); U.C.C. § 5-116 cmt. 3 (stating that, if there is no conflict between Article 5 and incorporated rules of practice, both apply).

152. *See* U.C.C. § 5-103, cmt. 2 ("Normally Article 5 should not be considered to conflict with practice except when a rule explicitly stated in the UCP or other practice is different from a rule explicitly stated in Article 5."). *But see* James E. Byrne & Lee H. Davis, *New Rules for Commercial Letters of Credit Under UCP 600*, ANN. SURV. LETTER OF CREDIT L. & PRAC. 29, at 49-51 (Byrne & Byrne ed. 2008) (stating that the UCP 600 definition of negotiation can not vary the Article 5 concept of value without explicitly so providing).

153. *See PTZ Trading Ltd.*, 768 N.E. 2d at 637 (stating that, if the UCP has no rule upon a particular topic, incorporation of the UCP does not displace the Article 5 rule).

The incorporation of UCP 600 into a letter of credit subject to Article 5 alters the following variable Article 5 rules: (1) the Article 5 maximum seven-business-day deadline for examination of presented documents is reduced to a maximum of five banking days;[154] (2) a nominated person that has opted to negotiate is subject to both the UCP 600 maximum five-banking-day deadline for examination of a presentation and the separate UCP 600 five banking-day-deadline for giving expeditious notice of discrepancies;[155] and (3) notice of refusal of the presented documents must be given by expeditious means.[156]

UCP 600's silence as to whether its deadline for examination of documents can give rise to preclusion does not displace the explicit Article 5 rules that a reasonable time for document examination can expire before the outside deadline and that preclusion can arise from dilatory examination.[157] On the other hand, UCP 600's imposition of these deadlines upon nominated persons acting upon their nominations is hortatory. Nominated persons are not subject to either UCP 600 or Article 5 preclusion.[158]

The incorporation of ISP 98 into a letter of credit subject to Article 5 supplements the Article 5 requirement of timely notice of refusal to honour upon completion of document examination within a maximum seven-business-day period. ISP 98 adds the unrebuttable presumptions that notice given within three business days after the business day of presentation is reasonable and that notice given more than seven business

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154. *Compare supra* note 79 and accompanying text (discussing Article 5 deadline), *with* discussion and accompanying text, *supra* note 122 (discussing UPC 600 deadline).

155. The UCP 600 rules imposing these deadlines expressly state that they apply to nominated banks acting upon their nominations. *See* UCP 600, *supra* note 7, art. 14(b) (indicating that a nominated bank acting on its nomination has a maximum of five banking days to examine the documents); *id.* art. 16(d) (indicating that a nominated bank acting upon its nomination has a maximum of five banking days to give notice of refusal to the presenter). Article 5 excludes nominated persons from its counterpart rules. *See* U.C.C. § 5-108, cmt. 6 (stating that this section does not impose duties upon a person that is not the issuer or a confirmer).

156. *See* UCP 600, *supra* note 7, art. 16(d) (notice of refusal of the documents must be given by expeditious means). Article 5 merely requires notice within its maximum seven-business-day deadline. *See* discussion and accompanying text, *supra* notes 79-81.

157. *See* U.C.C. § 5-116(c) (providing that only "conflicting" rules of practice displace Article 5 variable rules); *see also* discussion and accompanying text, *supra* notes 133-134 (discussing whether the UCP 600 deadline for examination of documents gives rise to UCP 600 preclusion).

158. UCP 600, *supra* note 7, art. 16(f); U.C.C. § 5-108, cmt. 6. *See also* discussion and accompanying text, *supra* notes 85, 131 (discussing the absence of Article 5 and UCP 600 preclusion rules with respect to nominated persons and nominated persons' liability to the beneficiary for breach of contract and inducing prejudicial reliance).

days after the business day of presentation is unreasonable, plus the requirement that notice of refusal must be given by expeditious means.[159]

IV. THE NATURE OF A NEGOTIATION CREDIT

A. Necessary Terms

Neither Article 5 nor UCP 600 nor ISP 98 define a negotiation credit.[160] But, UCP 600 includes a new definition of "negotiation,"[161] which will be influential under the other regimes, and all three regimes authorize the issuer to nominate a person or persons "to negotiate" the documents required by the issuer's letter of credit.[162] The persons nominated to negotiate are typically banks,[163] and will be referred to as "nominated negotiating banks".

The nature of a negotiation credit has been adumbrated primarily by judicial decisions in the United States, the United Kingdom, the Commonwealth of Nations,[164] and jurisdictions like Hong Kong that

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159. OFFICIAL COMMENTARY ISP 98, *supra* note 8, rule 5.01(a)(i). *See also* discussion and accompanying text, *supra* notes 140-144.

160. *See* U.C.C.§ 5-102(a) (omitting negotiation credit from the list of definitions); UCP 600, *supra* note 7, art. 2 (omitting negotiation credit from the list of definitions); OFFICIAL COMMENTARY ISP 98, *supra* note 8, Rule 1.09 (omitting negotiation credit from the list of definitions). A letter of credit is not per se a negotiable instrument. *See, e.g.*, Bank of China v. Chan, 937 F.2d 780, 783 (2d Cir. 1991) (holding that letters of credit are not negotiable instruments). The term negotiation credit is derived from the fact that negotiation credits formerly used to include negotiable drafts as required documents. *See* John F. Dolan, *How Negotiation Letters of Credit Can Go Wrong*, 17 BANKING & FIN. L. REV. 129 (2001) (stating that negotiable drafts drawn by the beneficiaries of negotiation credits gave the credit its name); *see also supra* note 13 (defining "draft").

161. *See* UCP 600, *supra* note 7, art. 2 (defining "negotiation"); *see also infra* notes 214-258 and accompanying text (discussing the new definition of "negotiation").

162. *See* U.C.C. § 5-102(a) (11) (nominated persons include a person authorized by the issuer to negotiate the letter of credit whom the issuer has undertaken to reimburse); UCP 600, *supra* note 7, art. 12(a) (stating that a nominated bank can be authorized to negotiate); OFFICIAL COMMENTARY ISP 98, *supra* note 8, 2.04(a) (stating that a standby can nominate a person to negotiate).

163. UCP 600 reflects this by referring exclusively to nominated banks. *See* UCP 600, *supra* note 7, art 2 (referencing "nominated bank" in the definition of "negotiation").

164. The British Commonwealth, now known as the Commonwealth of Nations, comprises the United Kingdom, former dependences that have become independent, and remaining dependencies like Bermuda. *See* COMMONWEALTH SECRETARIAT, MEMBER STATES, *available at* http://www.thecommonwealth.org/Internal/142227/members/ (last visited Nov. 18, 2008) [hereinafter MEMBER STATES]. Mozambique is the only member that was not formerly a British colony. *See* COMMONWEALTH SECRETARIAT, MOZAMBIQUE HISTORY, *available at* http://www.thecommonwealth.org/YearbookInternal/145170/-history/ (last visited Nov. 18, 2008). Singapore is a member of the Commonwealth and

apply principles of English commercial law.[165] The substantive significance of a negotiation credit[166] requires a clear expression of the intention to create one. In order to be a negotiation credit, a letter of credit must contain both a clear undertaking by the issuer to reimburse a nominated negotiating bank that has negotiated and a clear identification of the bank or banks nominated to negotiate.[167]

Various formulations have been recognized. If drafts are among the required documents, a traditional clause provides that "[the issuer] agree[s] with the drawers, endorsers and bona fide holders of drafts drawn under, and in compliance with the terms of this letter of credit that the same *shall be duly honored upon presentation and delivery of the*

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the Singapore courts have decided a number of cases involving negotiation credits. *See* MEMBER STATES, *supra*.

165. Hong Kong became a Special Administrative Region of the People's Republic of China following the end of British rule in 1997 and could not join the Commonwealth. *See* Details, HCCH, Hague Conference on Private International Law, *available at* http://hcch.e-vision.nl/index_en.php?act=status.comment&csid=914+disp=resdn (last visited Nov. 18, 2008). However, Chapter 1, Article 8 of the Basic Law of the Hong Kong Special Administrative Region provides: "[t]he laws previously in force in Hong Kong, that is, the common law, rules of equity, ordinances, subordinate legislation and customary law shall be maintained, except for any that contravene this Law, and subject to any amendment by the legislature of the Hong Kong Special Administrative Region." International Constitutional Law, Hong Kong- Constitution, *available at* http://www.constitution.org/cons/hongkong.txt (last visited Nov. 18, 2008).

166. The beneficiary, for example, can make a timely presentation of conforming documents to a negotiating bank and a negotiating bank that has negotiated the documents in good faith and without notice takes free of remedies for material fraud. U.C.C. § 5-109(a)(1)(i). *See also infra* notes 186-190 and accompanying text. Moreover, the rights of a holder in due course of a negotiable instrument drawn under a negotiation credit will not necessarily be recognized. *See supra* note 101 and accompanying text.

167. *See, e.g.*, First Commercial Bank v. Gotham Originals, Inc., 475 N.E.2d 1255, 1260 (N.Y. 1985) (involving an express "engagement in the letter of credit to honor drafts presented by a negotiating bank"). Like Article 5, Old Article 5 also referred to negotiation and negotiating banks but did not define negotiation credit. *See* U.C.C. § 5-103 (1962) (providing no definition of negotiation credit); U.C.C. § 5-114(2)(a) (referring to "negotiating bank"); DOLAN TREATISE, *supra* note 12, Appendix B, at App. B-4, B-5, B-19. *See also* European Asian Bank v. Punjab & Sind Bank, [1983] 1 Lloyd's Rep. 611, 613 (C.A.) ("We hereby engage with the drawers, endorsers and bona fide holders of drafts drawn under and in compliance with the terms of this credit that such drafts shall be duly honoured on presentation and delivery of documents as specified above . . . negotiations under this credit are restricted to [address]."); Cruickshank v. Westpac Banking Corp., [1989] 1 N.Z.L.R. 114, 117 (H.C. Auckland 1988) ("[I]n Auckland, New Zealand for negotiation. . . . We hereby engage with the drawers and/or bona fide holders that drafts drawn and negotiated in conformity with the terms of this credit will be duly honoured on presentation and that drafts accepted within the terms of this credit will be duly honoured at maturity."); Cooperative Centrale Raiffeisen-Boerenleenbank v. Bank of China, HCCL 56/2001 [2004], *available at* http://legalref.judiciary.gov.hk/lrs/-common/ju/judgment.jsp (last visited Nov. 18, 2008).

documents herein specified."[168] A more contemporary approach is for the issuer to check the box in the letter of credit stating that the credit is "available by negotiation".[169] A letter of credit without a clear undertaking and identification is a "straight letter of credit" (a "straight credit"), and not a negotiation credit.[170]

Confirmation is not negotiation. A negotiation credit does not require confirmation.[171] Furthermore, confirmation of a straight credit that does not nominate a negotiating bank makes the letter of credit available with the confirmer as well as the issuer but does not create a negotiation credit.[172]

Vague, general references to "negotiation" in a letter of credit do not create a negotiation credit.[173] In *Credit Agricole Indosuez v. Banque*

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168. Algemene Bank Nederland v. Soysen Tarim Urunleri Dis Ticaret Ve Sanayi, A.S., 748 F. Supp. 177, 182 n.6 (S.D.N.Y. 1990) (emphasis in original) (identifying the clause as creating a negotiation credit). Professor Dolan considers that this type of clause creates a "circular negotiation credit" that is freely negotiable by any third party. *See* DOLAN TREATISE, *supra* note 12, at 1-11 (explaining that a negotiation credit that nominates any bona fide holder of drafts drawn under it is a "circular negotiation credit"). A more modern form of circular negotiation credit restricts the nominated persons to banks. *E.g.*, "drafts are available by negotiation with any bank." *See id.*

169. *See* WHITE & SUMMERS TREATISE, *supra* note 101, at 194 (explaining that, if the "negotiation" block is checked,. the document is a negotiation credit).

170. *Compare* DOLAN TREATISE, *supra* note 12, ¶ 10.02[2] (explaining that a "straight" credit runs only to the beneficiary), *with* WHITE & SUMMERS TREATISE, *supra* note 101, at 193-94 (distinguishing between negotiation credits and credits that are not negotiation credits).

171. *See* Amixco Asia Ltd v. Bank Bumiputra, [1992] 2 S.L.R. 943, 947 (Sing. H.C.) (holding that an unconfirmed negotiation credit was an undertaking only by the issuer).

172. *See, e.g., Banco Santander*, [2000] 1 ALL E.R. (Comm.) at 777-78, 785-86 (holding that confirmation of a straight deferred payment letter of credit did not create a negotiation credit authorizing the confirming bank to purchase its own deferred payment obligation from the beneficiary prior to its maturity). UCP 600 contains a provision that deems a bank nominated to accept a time draft or to incur a deferred payment undertaking to be authorized to prepay or to purchase its own acceptance and its own deferred payment undertaking. *See infra* notes 259-285 and accompanying text. This provision effectively reverses the holding of *Banco Santander* without making the letter of credit a negotiation credit.

173. *See, e.g.*, Udharam Rupchand Sons v. Mercantile Bank, HCCL 24/1984 [1985] H.K. H.C., ¶¶ 64-80, *available at* http://legalref.judiciary.gov.hk/lrs/common/ju/-judgment.jsp (last visited Nov. 18, 2008), *appeal dismissed*, 1985 WL 549394 (H.K. C.A. 1985) (alternative holding) (recognizing that three general references to either "negotiation" or "negotiating" are immaterial where the letter of credit did not spell out an engagement to reimburse third-party banks); *accord Credit Agricole Indosuez*, [2001] 2 S.L.R. 1, at 8-13 (alternative holding) (recognizing three general references to "negotiation" and requiring the presentation of drafts as insufficient to make up for the absence of a clear and explicit engagement clause in favor of third parties). In dictum, the *Credit Agricole* court observed that a reference to "negotiation is permitted" plus a clause

Nationale,[174] the Singapore Court of Appeal, for example, reversed a lower court determination that Banque Nationale was a negotiating bank. Because a standard letter of credit does not provide for negotiation, the Court of Appeal panel reasoned that the intention to issue a negotiation credit should be clear and explicit.[175] In dictum, the panel observed that the language "negotiation is permitted," standing alone, would be insufficient,[176] and went on to hold that three general references to "negotiation" plus requiring the presentation of drafts did not created a negotiation credit.[177]

A negotiation credit must identify the nominated negotiating banks. The following traditional clause, for example, runs to all banks and nonbanks that are bona fide holders of drafts drawn under and in compliance with the letter of credit: "[the issuer] agree[s] with the drawers, indorsers and bona fide holders of drafts drawn under, and in compliance with the terms of this letter of credit that the same *shall be duly honored upon presentation and delivery of the documents herein specified.*"[178]

The nomination to negotiate can be to "any bank,"[179] or restricted to any bank in a designated country or city,[180] or to a single office of a

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stating that "we hereby undertake to honour all drafts drawn under and in conformity with the terms of the credit" would not create a negotiation credit. *Id.* at 12.

174. [2001] 2 S.L.R. 1 (Sing. C.A.). The Court of Appeals is Singapore's highest and final appellate court. *See* Supreme Court of Singapore, Our Courts, *available at* http://app.supremecourt.gov.sg/default.aspx?pgID=43 (last visited Nov. 18, 2008).

175. *Credit Agricole Indosuez*, [2001] 2 S.L.R. at 12 ("[A]ll letters of credit are addressed specifically to the seller/beneficiary, and, absent clear language to the contrary, are confined to the seller/beneficiary.") (quoting JUDAH P. BENJAMIN, BENJAMIN'S SALE OF GOODS (5th ed. 1997)).

176. *Id.*

177. *Id.* at 9-13 (holding that three general references to negotiation, and drafts being required did not create a negotiation credit). The Court of Appeal also pointed out that Banque Nationale had endorsed the letter of credit "non-negotiable" before forwarding it to the beneficiary and had not expressly advised the issuer that Banque Nationale had negotiated the required documents. *Id.* at 13-14 (Banque Nationale appeared to have negotiated the documents on its own). *See also Udharam Rupchand Sons*, HCCL 24/1984 [1985] H.K (holding three oblique references to "negotiation" or "negotiating" insufficient to create a negotiation credit).

178. *Algemene Bank Nederland*, 748 F. Supp. at 182 (emphasis in original).

179. *See* U.C.C. § 5-102, cmt. 7 (referring to clause providing "available with any bank by negotiation"). Professor Dolan describes a letter of credit that can be negotiated by any bank as a "circular negotiation credit." DOLAN TREATISE, *supra* note 12, at 1-11.

180. *See* RAYMOND JACK, ALI MALEK & DAVID QUEST, DOCUMENTARY CREDITS Appendix 5 Standard Document 2 (3d ed. 2001) (presenting SWIFT Format letter of credit available by negotiation with "any bank in Taiwan").

single bank.[181] Nevertheless, an issuer's acknowledgement that an advising bank that had not been nominated could negotiate, followed by that bank's prejudicial reliance upon the acknowledgment, estops the issuer to refuse reimbursement.[182]

A letter of credit providing for payment at sight by the issuer or a confirmer can be a negotiation credit.[183] So can a letter of credit providing for the acceptance of time drafts by the issuer or a confirmer[184] or for a deferred payment undertaking by the issuer or a confirmer.[185]

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181. *See* European Asian Bank v. Punjab & Sindh Bank, [1983] 1 Lloyd's Rep. 611, 613 (C.A. 1983) ("[N]egotiations under this credit are restricted to Algemene Bank Nederland NV 2 Cecil Street Corner 'd Almeida Street, P.O. Box 493, Singapore-1"). However, the United Kingdom Court of Appeal ruled that the issuer had waived the exclusivity of the negotiation clause by responding to a notice of negotiation and presentation of documents by an advising bank that the applicant had accepted the documents presented. *Id.* at 619-21 (holding that the issuer unequivocally had represented to the presenter that it was entitled to negotiate the documents and that the documents had been in order). Professor Dolan describes a negotiation credit that nominates a single bank as a "domiciled negotiation credit." *See* DOLAN TREATISE, *supra* note 12, at 1-11 (holding negotiation credits that nominate a single bank to negotiate are "domiciled").

182. *See European Asian Bank*, [1983] 1 Lloyd's Rep. at 613, 619-21 (recognizing issuer estopped from asserting that the advising bank had not been nominated to negotiate the required documents after assuring the advising bank that the applicant had accepted the documents and the advising bank had allowed the beneficiary to withdraw the credit with which the documents had been purchased). The issuer's or a confimer's failure to reject in timely fashion a presentation on its own behalf by a presenter that had not been nominated to negotiate would give rise to Article 5 and UCP preclusion to assert the lack of nomination notwithstanding the presenter's failure to rely prejudicially upon the failure to reject the presentation in timely fashion. Article 5 and UCP preclusion do not require prejudicial reliance. U.C.C. § 5-108, cmt. 8 (emphasizing that statutory preclusion is not dependent upon principles of waiver and estoppel); UCP 600, *supra* note 7, art. 16(f) (stating that an issuing or a confirming bank that fails to act in compliance with Article 16 is precluded from claiming that the documents do not constitute a complying presentation). *See also European Asian Bank*, [1983] 1 Lloyd's Rep. at 620 (advising bank asserted the preclusion provision in UCP 300 in addition to its claim of estoppel).

183. *See, e.g.*, Chinsim Trading Ltd. v. Indian Bank, [1993] 2 S.L.R. 144, 146-47 (Sing. H.C. 1993) (involving an unconfirmed letter of credit containing an undertaking to reimburse "on receipt of documents" and a commitment by the issuer to bona fide holders of drafts drawn and negotiated under the letter of credit).

184. *See, e.g.*, Indian Bank v. Union Bank, [1994] 2 S.L.R. 121, 123-24 (Sing. C.A. 1994) (involving an amended letter of credit providing for time drafts payable 120 days from the bill of lading date drawn upon and accepted by the confirmer and containing a commitment from the issuer and the confirmer to bona fide holders of drafts drawn and negotiated under the letter of credit).

185. *See* Czarnikow-Rionda Sugar Trading, Inc. v. Standard Bank, [1999] 2 Lloyd's Rep. 187, 193-95, 205-06 (Q.B.D. Comm.) (noting that the deferred payment letters of credit appeared to nominate two banks as both confirming banks and negotiating banks); *see also Banco Santander*, [2000] 1 All E.R. (Comm.) at 786 (suggesting in dicta that the result would have been different if the bank confirming the deferred payment credit also had been authorized to negotiate). *But see* Credit Agricole Indosuez v. Bank Nationale,

B. The Significance of Negotiation

If a nominated negotiating bank acts upon its nomination to negotiate, there are significant consequences. The nominated bank, for example, can present the required documents for reimbursement in its own name.[186] Furthermore, as long as the beneficiary made a timely conforming presentation to the nominated negotiating bank, the issuer and a confirmer are obligated to reimburse the negotiating bank even though the issuer or the confirmer did not receive the request for reimbursement and the required documents until after the expiration of the deadline for the presentation of shipping documents or even after the expiration of the letter of credit.[187] Indeed, some negotiation credits expressly designate an expiration date and an earlier deadline for presentation of shipping documents as the last date for negotiation of the documents subject to the deadline.[188] A nominated negotiating bank that

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[2001] 2 S.L.R. 1, 8-14 (Sing. C.A.) (treating deferred payment credits and negotiation credits as mutually exclusive categories). However, the court's conclusion that a deferred payment straight credit was involved was influenced by the alleged nominated negotiating bank's having regarded the credit as a straight credit prior to the litigation. *Id.* at 13-14 (confirming and advising bank had endorsed "non-negotiable" upon the letter of credit before forwarding it to the issuer).

186. *See* U.C.C. § 5-107, cmt. 4 (stating that, in a freely negotiable credit, the issuer agrees to pay the nominated banks that negotiate conforming documents); *see also Cooperative Centrale Raiffeisen-Boerenleenbank*, [2004] 3 H.K.L.R.D. at ¶¶ 70-85, (holding that negotiation had not taken place and the nominated negotiating bank was not entitled to assert a claim on the letter of credit in its own right).

187. *See* U.C.C. § 5-107, cmt. 4 (stating that nomination allows the beneficiary to present the documents to the nominated person instead of the issuer). However, this is the case only if a timely presentation of conforming documents had been made to the nominated negotiating bank. *Id.* The nominated bank's agreement that a defective presentation would be regarded as conforming is not binding upon the issuer or a confirmer. *See* Chinsum Trading (PTE) Ltd. v. Indian Bank, [1993] 2 S.L.R. 144, 149-50, 153 (Sing. H.C.) (holding that the issuer is not bound by the nominated negotiating bank's unjustified agreement with the beneficiary that presentation had been made prior to the expiration of the letter of credit). Letters of credit ordinarily contain express expiration dates. *See, e.g.*, Courtaulds North America, Inc. v. North Carolina Nat'l Bank, 387 F. Supp. 92, at 94 (M.D.N.C. 1975), *rev'd on other grounds*, 528 F.2d 802 (4th Cir. 1975) (holding in this Old Article 5 case that the letter of credit had been issued on March 3, 1973 and initially had provided that it would expire on June 15, 1973). If there is no stated expiration date, Article 5 provides one. *See* U.C.C. § 5-106(c) (providing that letter of credit without a stated expiration date expires either one year after its stated date of issue, or, if there is no stated date of issue, one year after the date of issue).

188. *See, e.g., European Asian Bank*, [1983] 1 Lloyd's Rep. at 613 ("[D]ocuments must be presented for negotiation within 15 days from the date of shipment."). UCP 600 deems an expiry date for negotiation to be an expiry date for presentation of documents. *See* UCP 600, *supra* note 7, art. 6(d)(i) (stating that an expiry date for honour or negotiation will be deemed to be an expiry date for presentation of documents).

had given the beneficiary value in good faith and without notice of material fraud for a conforming presentation is also not subject to a material letter-of-credit fraud defense that the issuer or a confirmer has against the beneficiary,[189] or to an action by the applicant to enjoin reimbursement.[190]

C. Determining whether Negotiation has Occurred

In rare cases, the issuer's authorization of a bank to examine a presentation of documents is coupled with an authorization for the bank to act as the agent of the issuer instead of as a negotiating bank.[191] A beneficiary also can instruct a nominated negotiating bank merely to collect the documents from the issuer or a confirmer without negotiation.[192] The beneficiary's application for negotiation by a nominated negotiating bank, moreover, may or may not be accepted. A nominated negotiating bank that has not agreed to negotiate is free to decline to act upon its nomination.[193]

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189. *See* U.C.C. § 5-109(a)(1)(i) (stating that notwithstanding evidence of material fraud or forgery, the issuer must honor a presentation by a nominated person that has "given value in good faith and without notice of the material forgery or fraud"); *see also* U.C.C. § 5-107, cmt. 4 (stating that a nominated person has rights to payment that others do not enjoy); U.C.C. § 5-109, cmt. 6 (stating that a letter of credit nominating a person to negotiate induces the nominated person to give value and can entitle the nominated person to protection from the issuer's material fraud defense). Proof of material fraud or forgery can justify good faith dishonor by the issuer or a confirmer notwithstanding the apparent facial conformity of a documentary presentation. U.C.C. § 5-109(a)(2) (stating that an issuer, acting in good faith, can dishonor for material fraud a presentation by an unprotected person).

190. *See, e.g.*, Brenntag Int'l Chemicals, Inc. v. Bank of India, 175 F.3d 245, 250-52 (2d Cir. 1999) (affirming preliminary injunction restraining a nominated negotiating bank from pursuing unjustified attempts to obtain honor of a standby letter of credit); *see* U.C.C. § 5-109(b) (authorizing an applicant to seek an injunction against honor of a presentation of documents by the issuer and similar relief against reimbursement in the event of material letter-of-credit fraud).

191. *See* U.C.C. § 5-107, cmt. 4 (stating that, in rare cases, a nominated person also is an agent of the issuer); S. Ocean Shipbuilding Co. v. Deutsche Bank, 1993 3 S.L.R. 686, 692-96 (Sing. H.C.) (holding that Eastern Asian Bank Singapore had been designated as the issuer's agent to examine the compliance of the documents and that the issuer was bound by Eastern Asia's wrongful dishonor).

192. *See, e.g.*, Nanyang Com. Bank v. Man Sam Kuan, HCMP 403/1999 [2006] H.K. C.F.I., ¶ 42, *available at* http://legalref.judiciary.gov.hk/lrs/common/ju/judgement.jsp (last visited Nov. 18, 2008), *appeal dismissed on other grounds*, CACV 418/2006 [2007] H.K. C.A., *available at* http://legalref.judiciary.gov.hk/lrs/common/ju/judgment.jsp (last visited Oct. 21, 2008) (noting that the beneficiary had instructed a nominated bank to collect the documents from the issuer).

193. *See* U.C.C. § 5-107(b); UCP 600, *supra* note 7, art. 12(c). *See also supra* notes 39, 121 and accompanying text.

If the beneficiary makes a timely presentation of the required documents to a nominated negotiating bank that neither is a confirmer nor has made a special agreement to negotiate and that bank refuses to negotiate, the timeliness of the presentation is not affected. Presentation consists of the receipt of the required documents at an authorized place.[194] Negotiation plays no part in it.[195] A nominated negotiating bank that does not choose to negotiate, moreover, ordinarily will act as a collecting bank for the beneficiary, presenting the documents to the issuer or a confirmer upon the beneficiary's behalf.[196] UCP 600 facilitates this by requiring the issuer and a confirmer to honour a letter of credit that is available with a nominated negotiating bank that has declined to negotiate.[197]

V. THE LIMITED ARTICLE 5 AND ISP 98 TREATMENT OF NEGOTIATION CREDITS

Although a few Official Comments discuss other aspects of negotiation credits,[198] Article 5 statutory treatment focuses upon the immunity from remedies for material letter-of-credit fraud of a nominated negotiating bank that has given value for the required documents in good faith and without notice of the fraud.[199] "Nominated

194. *See* U.C.C. § 5-102(a)(12) (defining presentation as delivery of a document to the issuer or a nominated person for honor or the giving of value); UCP 600, *supra* note 7, art. 2 (presentation means either the delivery of documents under a credit to the issuing bank or a nominated bank or the documents so delivered); *see also* COMPARISON UCP 600 & UCP 500, *supra* note 113, at 114-15 ("[P]resentation to a nominated bank on or before the expiration date is timely whether or not the bank elects to act on its nomination . . . .").

195. The receipt and the forwarding of documents by a nominated negotiating bank is not negotiation. UCP 600, *supra* note 7, art. 12(c) ("[R]eceipt or examination and forwarding by a nominating bank that is not a confirming bank does not . . . constitute honour or negotiation.").

196. *See, e.g.*, *Union Bank of Switzerland*, [1994] 2 S.L.R. at 128-132 (determining that a nominated negotiating bank had acted as a collecting bank).

197. UCP 600, *supra* note 7, arts. 7(a)(v), 8(a)(i)(e) (stating that the issuer and a confirmer have an obligation to honour if a nominated bank does not act upon its nomination to negotiate).

198. *See* U.C.C. § 5-102, cmt. 7 (discussing the significance of a nomination to negotiate); U.C.C. § 5-107, cmt. 4 (discussing the freedom of a nominated negotiating bank that is not a confirmer to refuse to act upon its nomination); U.C.C. § 5-108, cmts. 5, 6 (discussing nominated persons' rights as presenters and exclusion from the examination deadline and preclusion).

199. *See* U.C.C. § 5-109(a)(1)(i), cmt. 6 (explaining the importance of nomination for immunity from remedies for material letter-of-credit fraud).

person" is defined but "negotiation credit" and "negotiation" are not,[200] and confirmers are the only nominated banks that must undertake to give the value that they have been nominated to give.[201] Nevertheless, if a negotiation credit exists, a nominated negotiating bank that has given value in good faith and without notice of material letter-of-credit fraud is not subject to the issuer's or a confirmer's material fraud defense,[202] or to the applicant's action to enjoin reimbursement,[203] and can recover for the issuer's or a confirmer's wrongful dishonor.[204] In order to enhance the probability of honor, a confirmer that has honored its confirmation has greater protection. A confirmer has immunity from remedies for material letter-of-credit fraud as long as it had honored in good faith.[205] It is immaterial that the confirmer had had notice of alleged material fraud.[206]

ISP 98, Rule 2.04, dealing with nomination, is the principal ISP 98 treatment of negotiation credits. A standby can nominate a bank or banks to negotiate.[207] A nominated negotiating bank that has not undertaken to act is not obligated to do so.[208] Also, a nominated bank is not authorized to bind the person making the nomination.[209] Comment 3 to Rule 2.04

200. *See* U.C.C. § 5-102(a) (defining "nominated person" but not "negotiation" or "negotiation credit"). However, by generally defining a "nominated person" as a person entitled to be reimbursed for acting upon the authorization to give value under a letter of credit, the definition of nominated person signals that negotiation requires the giving of value under a letter of credit, which is similar to the UCP 500 concept of negotiation. *See* U.C.C. § 5-102(a)(11); UCP 600, *supra* note 7, art. 10(b)(ii) (stating that negotiation is "the giving of value for Draft(s) and/or documents by the bank authorized to negotiation" and "[m]ere examination without giving of value does not constitute a negotiation").

201. *See* U.C.C. § 5-107(a)-(b) (stating that confirmers, but not other nominated persons, are obligated to give value under a letter of credit).

202. U.C.C. § 5-109(a)(1)(i) (requiring the issuer and a confirmer to honor a conforming presentation by a nominated person that has given value in good faith and without notice of material fraud or forgery).

203. U.C.C. § 5-109(b)(4) (stating that, in order to obtain equitable relief against honor or reimbursement, an applicant must show that the person demanding honor or reimbursement is not immune from remedies for material letter-of-credit fraud).

204. U.C.C. § 5-111(a) (stating that a nominated person presenting required documents in its own behalf can recover for wrongful dishonor).

205. U.C.C. § 5-109(a)(1)(ii) (stating that the issuer shall honor the presentation of a confirmer that has honored its confirmation in good faith).

206. *Compare id., with* U.C.C. § 5-109(a)(1)(i) (stating that, in order to have immunity from remedies for material fraud, a nominated person must have "given value in good faith and without notice of forgery or material fraud" but that a confirmer only must have "honored its confirmation in good faith").

207. *See* OFFICIAL COMMENTARY ISP 98, *supra* note 8, rule 2.04(a) (listing various types of nominations).

208. *Id.* rule 2.04(b) (stating that nomination per se does not obligate the nominated person to act upon the nomination).

209. *Id.* rule 2.04(c) (stating that a nominated person can not bind the nominating person).

explains that a negotiation standby authorizes a nominated negotiating bank to purchase the required documents and to obtain reimbursement.[210] A negotiation standby must identify the banks nominated to negotiate. A freely negotiable standby nominates "any bank," but it is more common to nominate any bank in a particular city.[211] Unless the standby clearly indicates that it is freely negotiable, nomination is considered to be limited to the specific nominees.[212]

Coupled with Article 5's deference to most conflicting UCP provisions that have been incorporated into a letter of credit,[213] the limited Article 5 treatment of negotiation credits accommodates the UCP 600 definition of negotiation. ISP 98's minimal treatment of negotiation credits likewise could make the UCP 600 definition of negotiation influential with respect to negotiation standbys.

VI. THE UCP 600 DEFINITION OF NEGOTIATION

A. The Definition

UCP 600 defines "negotiation" as: "[T]he 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."[214] The definition requires the purchase of the required documents by advancing funds on or before the banking day on which reimbursement is due to the nominated negotiating bank.[215] If the letter of credit is to be honoured at sight, reimbursement is due following the issuer's or a confirmer's determination that there has been a conforming presentation.[216] Reimbursement for a conforming presentation under a letter of credit available by acceptance or by deferred payment is due upon the maturity

210. *Id.* rule 2.04, cmt. 3(a) (stating that a negotiation standby induces a nominated negotiating bank to purchase the required documents by providing for reimbursement).

211. *Id.* cmt. 3(b) (stating that freely negotiable standbys are rare).

212. *Id.* (requiring that free negotiability be clearly indicated).

213. *See* discussion and accompanying text, *supra* note 9 (discussing Article 5's express deference to most conflicting incorporated UCP 600 provisions).

214. UCP 600, *supra* note 7, art. 2. Recall that UCP 600 frequently uses terminology consistent with Article 5. However, the roles of adviser, issuer, nominated person, and confirmer are restricted to banks, time is measured in banking days, and honor and its derivatives are spelled "honour." *See* discussion and accompanying text, *supra* notes 49-52.

215. *Id.*

216. *See* discussion and accompanying text, *supra* notes 60, 111 (discussing honour under a letter of credit payable at sight).

of the accepted time draft or the deferred payment obligation.[217] The UCP 600 Drafting Group's Commentary emphasizes that the funding date of a nominated negotiating bank's executory promise to pay for the required documents must be no later than the estimated reimbursement date.[218] An agreement to advance funds only after their receipt from the issuer or a confirmer is not a UCP 600 negotiation.[219]

The amount of the purchase price is left to freedom of contract. If the letter of credit provides for acceptance of a time draft or a deferred payment obligation, at a minimum, a nominated negotiating bank will discount the amount paid to reflect the beneficiary's receipt of payment before it is due under the letter of credit.[220]

The definition states that an advance and a commitment to make an advance must be made "to" the beneficiary.[221] But there is no requirement that the advanced funds be paid to the beneficiary. It suffices that the funds are paid to the person or persons designated by the beneficiary.[222] A nominated negotiating bank's issue of a back-to-back

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217. UCP 600, *supra* note 7, arts. 7(c), 8(c) ("Reimbursement for the amount of a complying presentation under a credit available by acceptance or deferred payment is due at maturity . . . .").

218. *See* DRAFTING GROUP COMMENTARY UCP 600, *supra* note 7, at 22 ("[A] funding date [should be] set at or before the anticipated reimbursement date.").

219. *Id.* ("An agreement to advance funds if and when funds are received from the issuing bank is not negotiation . . . ."). *See also* Jim Barnes, *UCP 600 and Bank Responsibility for Fraud*, 13 No. 1 DC INSIGHT 5, 6 (Jan./Mar. 2007) ("An agreement to advance funds if and when funds are received from the issuing bank is not 'negotiation.'").

220. *See European Asian Bank*, [1983] 1 Lloyd's Rep. at 619 (noting that the negotiating bank had discounted the time draft that it had been advised was accepted by the applicant); *cf. Banco Santander*, [2000] 1 All E.R. at 777-78, 785-76 (holding that a confirming bank that had become obligated upon a deferred payment obligation had discounted its own obligation without authority and was subject to the issuer's material letter-of-credit fraud defense; dictum indicating the result would have been different if the confirming bank had been nominated to negotiate the documents). A back-to-back letter of credit is smaller in amount than the primary letter of credit to which it relates. If the only agreed purchase price for the documents required by the primary letter of credit is issue of a back-to-back letter of credit by a nominated negotiating bank, the negotiating bank acts as a collecting bank for the balance of the amount due under the primary letter of credit. *See Nanyang Com. Bank*, HCMP 403/1999 [2006] H.K. C.F.I. at ¶¶ 27-44, 48 (holding nominated negotiating bank, which had issued and honored a $652,015 back-to-back letter of credit in order to purchase the documents required by the $764,362 primary letter of credit would act as a collecting bank with respect to the amount of the primary letter of credit that it had not purchased). *See infra* notes 223-225 and accompanying text (discussing back-to-back letters of credit).

221. *See* UCP 600, *supra* note 7, art. 2 ("Negotiation means the purchase . . . by advancing or agreeing to advance funds to the beneficiary . . . .").

222. This is commonly done. *See* KING TAK FUNG, LEADING COURT CASES ON LETTERS OF CREDIT 69-70 (ICC Pub. No. 658 2004) ("In many jurisdictions, it is an acceptable

letter of credit, for example, can involve a UCP 600 agreement with the beneficiary to advance funds in the future. In a back-to-back letter of credit situation, the seller that is the beneficiary of the primary letter of credit, letter of credit #1, uses its rights under letter of credit #1 by pledge or otherwise to induce a nominated negotiating bank under letter of credit #1 to issue letter of credit #2 for a lesser amount in favor of the seller's supplier.[223] With the exception of the required invoice, the documents required by letter of credit #2 are usually those required by letter of credit #1.[224] As long as letter of credit #2 is honored prior to any deadline for the presentation of shipping documents and the expiration date in letter of credit #1, the nominated negotiating bank can obtain reimbursement under letter of credit #1 for its advance to the seller's supplier under letter of credit #2.[225]

B. Exclusions from the Definition

The exclusion of the purchase of drafts drawn upon the nominated bank from the definition of negotiation derives from negotiable instrument law. Under U.C.C. Article 3, "negotiation" is the transfer of

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practice that the negotiation proceeds be utilized without first crediting the beneficiary's account . . . .").

223. *See* DOLAN TREATISE, *supra* note 12, at G-4 (stating that the second or back-to-back letter of credit is issued in favor of the supplier of the beneficiary of letter of credit #1); *see, e.g., Cooperative Centrale Raiffeisen-Boerenleenbank*, 3 H.K.L.R.D. at ¶¶ 2-13 (noting that Jialing was the beneficiary of letter of credit #1 issued by Bank of China and the applicant for letter of credit #2 issued by Cooperative Centrale, a nominated negotiating bank under letter of credit #1, in favor of Jialing's supplier).

224. *See* WALTER BAKER & JOHN F. DOLAN, USER'S HANDBOOK FOR DOCUMENTARY CREDITS UNDER UCP 600, 83 (ICC Pub No. 694 2008) (stating that a back-to-back letter of credit requires the invoice of the seller's supplier; whereas the primary letter of credit requires the invoice of the seller).

225. *See* UCP 600, *supra* note 7, art. 2 (stating that for negotiation to occur a nominated negotiating bank must promise to "advance funds on or before the banking day on which reimbursement is due to the nominated bank"); art. 7(c) ("An issuing bank undertakes to reimburse a nominated bank" when the issuing bank's letter-of-credit undertaking is mature). *But see Cooperative Centrale Raiffeisen-Boerenleenbank*, 3 H.K.L.R.D. at ¶¶ 70-85 (holding issue and honor of a back-to-back letter of credit were not sufficient value for negotiation under UCP 500). The *Centrale Raiffeisen* case is not persuasive under UCP 600 for several reasons: (1) the judge considered that negotiation required the advancing of funds without recourse by a negotiating bank; and (2) the issuer of the back-to-back letter of credit failed to document that it had been issued and honored as the agreed purchase price for the documents required by letter of credit #1. *Id.* The record documentation included a collection order and an assignment of rights by the beneficiary of letter of credit #1 to the alleged negotiating bank and the record of the alleged negotiating bank's booking the payment of letter of credit #2 as an unsecured loan to the beneficiary of letter of credit #1. *Id.*

the possession of an issued negotiable instrument with all necessary indorsements so as to make the transferee the "holder."[226] Unlike UCP 600 negotiation,[227] Article 3 negotiation does not require that the transferee pay anything. Moreover, under Article 3, the bank upon which a draft is drawn would dishonor the draft after it had been presented for acceptance or payment by negotiating the draft to another. In order to avoid dishonor, following presentment for payment, the bank upon which a demand draft[228] has been drawn must pay the demand draft upon the day of presentment.[229] The bank, upon which a time draft was drawn, must accept the time draft upon the day of presentment for acceptance and pay the accepted time draft upon the day of presentment for payment on or after the maturity date.[230]

A letter of credit can require that drafts be drawn upon a specific office of the issuing bank.[231] Other offices of the issuing bank can be nominated to negotiate the required documents.[232] A confirming bank also can negotiate drafts drawn upon the issuing bank. However, the exclusion applies both to a confirming bank that had been nominated to

226. *See* U.C.C. §§ 3-201(a)-(b) (explaining that negotiation of an issued negotiable instrument, which requires the endorsement by any identified person to whose order it is payable, makes the transferee the holder of the negotiable instrument).

227. *Compare id.*, *with* UCP 600, *supra* note 7, art. 12, *and* UCP 500, *supra* note 7, art. 1. *See* discussion and accompanying text, *supra* note 214.

228. "A draft is payable upon demand if it states that it is payable upon demand or at sight, or otherwise indicates that it is payable at the will of the holder, or does not state any time of payment." U.C.C. § 3-108(a).

229. *See* U.C.C. § 3-502(b)(2) (explaining that a demand draft that is presented for payment is dishonored if not paid upon the day of presentment).

230. U.C.C. §§ 3-502(b)(3)-(4); (d)(2) (stating that a time draft is dishonored if not accepted upon the day of presentment for acceptance and paid upon the date of presentment for payment on or after the maturity date).

231. *See, e.g.*, *Jian Sing Bank*, 82 C.F.I. 2000, ¶¶ 11-12 ("[D]raft(s) for full invoice value drawn at 90 days after sight on credit issuing bank bearing the clause 'drawn under documentary credit no LC80010073 of Jain Sing Bank.' . . . All documents must be presented in one set via your banker to us at [address]"); *see* U.C.C. § 4-107 (stating that a separate office is a separate bank for the purpose of determining the place at which action may be taken); *see generally* Dolan, *supra* note 1, at 60 (stating that drafts under negotiation credits are almost always drawn upon the issuer).

232. *See* U.C.C. § 5-116(b) ("[F]or purposes of jurisdiction, choice of law, and recognition of interbranch letters of credit, . . . all branches of a bank are considered separate entities."); UPC 600, *supra* note 7, art. 3 (stating that branches of a bank in different countries are considered to be separate banks). Professor Byrne observed that UCP 600 art. 3 "uses the term 'branch' . . . in a generic sense that would encompass any relationship between any two offices of a bank . . . ." COMPARISON OF UCP600 & UCP500, *supra* note 113, cmt. 6, at 55. *See also* OFFICIAL COMMENTARY ISP 98, *supra* note 8, rule 2.02 (stating that an issuer's branch, agency, or other office acting or undertaking to act under a standby in a capacity other than as issuer is obligated in that capacity only and shall be treated as a different person).

negotiate and to an issuing bank that is presented with a draft drawn upon the office to which the draft is presented.[233]

Because it derives from negotiable instrument law, this exclusion literally applies only if a required document is a negotiable draft ordering either the issuing bank or a confirming bank to pay that has been presented to the bank ordered to pay. However, a U.C.C. Official Comment invites the courts to apply Article 3 negotiable instrument rules by analogy to nonnegotiable drafts.[234] The exclusion has no application to required documents that are not drafts.[235]

UCP 600 also provides that the "[r]eceipt or examination and forwarding of documents by a nominated bank . . . does [not] . . . constitute . . . negotiation."[236] This exclusion derives from the substantive requirement that negotiation involve the purchase of the required documents by a nominated negotiating bank.[237]

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233. *See* Credit Agricole Indosuez v. Muslim Commercial Bank, [2000] 1 Lloyd's Rep. 275, 276 (C.A.) (confirming bank had accepted draft drawn upon it under a letter of credit); *see also Comments from Canada and Saudi Arabia*, 11 No. 1 DC INSIGHT 16,17 (Jan./Mar. 2005) (suggesting that a confirming bank can not negotiate drafts drawn upon the confirming bank). By the same token, the issuing bank can not negotiate drafts drawn upon the issuing bank. *See* discussion and accompanying text, *supra* notes 226-230. A confirming bank is a nominated bank that has accepted the issuing bank's invitation to confirm. *See* discussion and accompanying text, *supra* notes 39-40.

234. *See* U.C.C. § 3-104, cmt. 2. Comment 2 to Section 3-104 states:

> An order . . . that is excluded from Article 3 . . . may nevertheless by similar to a negotiable instrument in many respects. . . . [N]othing in Section 3-104 or in Section 3-102 is intended to mean that in a particular case involving such a writing a court could not arrive at a result similar to the result that would follow if the writing were a negotiable instrument.

Id. See also U.C.C. § 3-104, cmt. 2 ("[I]t may be appropriate . . . to apply one or more provisions of Article 3 to the writing by analogy [to orders to pay that are not negotiable instruments].").

235. *See* discussion and accompanying text, *supra* notes 226-230 (discussing the rationale for the exclusion under negotiable instruments law). In some transactions, the required documents do not include either a draft or a documentary demand. *See, e.g., Southern Ocean Shipbuilding Co.*, [1993] 3 S.L.R. at 689 (involving a deferred payment undertaking that required presentation of signed commercial invoices, packing lists, a signed letter of acceptance, a signed note confirming the dispatch date, and an insurance policy).

236. UCP 600, *supra* note 7, art. 12(c). UCP 500 combined both provisions in its concept of negotiation. *See* UCP 500, *supra* note 7, art. 10(b)(ii) ("[Negotiation is] the giving of value for Draft(s) and/or documents by the bank authorized to negotiate. Mere examination without giving of value does not constitute a negotiation.").

237. UCP 600, *supra* note 7, art. 2. *See also* discussion and accompanying text, *supra* note 214. The issuer and a confirmer are obligated to reimburse a nominated bank that has negotiated required documents when the issuer's or confirmer's undertakings are mature, which could be either upon receipt of conforming required documents or upon the maturity of a time draft or a deferred payment obligation. *See* UCP 600, *supra* note 7,

The reference to "the purchase . . . of drafts . . . and/or documents under a complying presentation"[238] excludes the purchase of noncomplying documents from UCP 600 negotiation.[239] A noncomplying presentation justifies the issuing bank's and a confirming bank's refusal to reimburse a nominated negotiating bank that purchased the documents.[240] But, an issuing bank and a confirming bank that failed, in timely fashion, to reject a noncomplying presentation by a nominated negotiating bank or that failed to specify actual documentary discrepancies as justifications for rejection would be precluded from asserting that the documents had not constituted a complying presentation.[241]

C. The Significance of Negotiation

1. The Article 5 Immunity from Remedies for Material Fraud of Nominated Negotiating Banks that have Negotiated

UCP 500 merely required that a nominated negotiating bank give "value"[242] for the documents, which had been consistent with the Article 5 concept of value.[243] The UCP 600 requirement that negotiation consist of a negotiating bank's purchase of the required documents by advancing

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art. 7(c) (describing issuer's reimbursement obligation); UCP 600, *supra* note 7, art. 8(c) (describing confirmer's reimbursement obligation).

238. *See* UCP 600, *supra* note 7, art. 2. A "complying presentation" is "a presentation that is in accordance with the terms and conditions of the credit, the applicable provisions of these rules and international standard banking practice." *Id.*

239. *See* COMPARISON OF UCP 600 & UCP 500, *supra* note 113, cmt. 12, at 36 (describing the exclusion as "unfortunate" as there is no necessary relationship between a complying presentation and negotiation); UCP 600, *supra* note 7, art. 15(c) (requiring a nominated negotiating bank that has negotiated to forward the documents to the issuing or a confirming bank, which would enable the issuing or confirming bank to determine whether the presentation is complying).

240. UCP 600, *supra* note 7, art. 7(c) (explaining that the issuing bank undertakes to reimburse only a nominated bank that has negotiated a complying presentation); UCP 600, *supra* note 7, art. 8(c) (explaining that a confirming bank undertakes to reimburse only a nominated bank that negotiated a complying presentation).

241. UCP 600, *supra* note 7, art. 16(f) (explaining that an issuing or a confirming bank that fails to act in accordance with art. 16 "shall be precluded from claiming that the documents do not constitute a complying presentation"). Notice of refusal to honour must be given "no later than the close of the fifth banking day following the day of presentation." UCP 600, *supra* note 7, art. 16(d).

242. *See* discussion, *supra* note 236.

243. U.C.C. § 5-102(b) (explaining that the definitions of value in U.C.C. §§ 3-303, 4-211 apply to Article 5). *See* discussion and accompanying text, *supra* notes 107-110 (discussing Article 5 concept of value).

funds to the beneficiary[244] is a substantive change that interfaces with the Article 5 immunity from remedies from material fraud of a nominated negotiating bank that has negotiated. The Article 5 immunity provision states that "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 . . . ."[245]

The UCP 600 definition of negotiation defines the value that suffices for negotiation differently than Article 5. Article 5 "value" includes the payment or securing of an antecedent debt owed to anyone, provisional credit that has been withdrawn or applied, provisional credit that is available for withdrawal as a matter of right, and an advance. However, an executory promise that is not embodied either in a negotiable instrument or in an irrevocable promise to a third party is not Article 5 value.[246] By requiring that the price paid for the required documents involve either a present advance or a future advance pursuant to commitment, UCP 600 rules out both the satisfaction and the securing of a prior debt as the purchase price.[247]

Although UCP 600 purports to describe negotiation as an agreement to make a timely future advance,[248] this is misleading. An agreement to make a future advance is only an executory negotiation.[249] Performance of the agreement to make a future advance is necessary to consummate the negotiation. If the applicant obtained an injunction against a nominated negotiating bank's funding its executory promise to pay the purchase price due to material fraud by the beneficiary, the nominated negotiating bank could not acquire immunity from remedies for the material fraud.[250]

The UCP 600 definition of negotiation does not address and does not affect the good faith, and without notice of material fraud, conditions of

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244. UCP 600, *supra* note 7, art. 2.

245. U.C.C. § 5-109(a)(1)(i).

246. U.C.C. §§ 3-303, 5-102(b).

247. *See* UCP 600, *supra* note 7, art. 2 (explaining that purchase involves either an advance or an agreement to advance in the future).

248. *See id.* (explaining that a promised advance must be due on or before the banking day upon which reimbursement is due).

249. *See* Jia Hao, *Rabobank v. Bank of China: A Warning and a Challenge to Banks' "Usual" Practice*, INST. INT'L BANKING L. & PRACT., 2007 ANN. SURV. LETTER OF CREDIT L. & PRAC. 75, 82 (2007) (explaining that negotiation requires performance of a promise to make an advance).

250. Jim Barnes, *UCP 600 and Bank Responsibility for Fraud*, 13 No. 1 DC INSIGHT 5, 7 (Jan./Mar. 2007) (explaining that the injunction would deprive the fraudulent beneficiary of funds without prejudicing the nominated negotiating bank that had been ordered by the court not to fund its commitment).

Section 5-109(a)(1)(i) immunity.[251] The alteration of the variable,[252] Article 5 concept of value, consequently is innocuous. The safeguards against material fraud are not lowered by recognizing performance of an executory promise to make a future advance as negotiation. If a nominated negotiating bank made either a present advance or a future advance that it was committed to the beneficiary alone to make, with either knowledge or reason to know of material fraud, the good faith and without notice conditions would preclude immunity.[253]

2. Negotiation with Recourse

A significant question is whether UCP 600 negotiation can occur if a nominated negotiating bank purchases the required documents "with recourse"—with the understanding that the beneficiary will repay the advanced funds upon demand if the issuer or a confirmer dishonors.[254]

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251. UCP 600, *supra* note 7, art. 2. The definition is silent with respect to the good faith and without notice of material fraud aspects of the immunity provision. *Id.*

252. *See* discussion, *supra* note 9 (listing the nonvariable Article 5 provisions).

253. *See PTZ Trading Ltd.*, 768 N.E. 2d at 634-37 (explaining that UCP 500 does not displace the Article 5 material fraud provisions for which it has no corresponding rules); *cf.* Rajaram v. Ganesh, [1995] 1 S.L.R. 159, 160-61 (Sing. H.C. 1994) (holding that the bank that was the nominal beneficiary of a guaranty had known at the time it had been enjoined from receiving payment that the actual beneficiary had not been entitled to be paid, which had vitiated the bank's right to receive the payment under the guaranty). On the other hand, if a nominated negotiating bank's executory promise had been made to a third party who had not been involved in the beneficiary's fraud, the executory promise could provide immunity. A nominated negotiating bank that had embodied its executory promise to the beneficiary in a back-to-back irrevocable letter of credit that had been issued prior to the negotiating bank's acquisition of knowledge or notice of material fraud by the beneficiary, for example, would be entitled to immunity even though the back-to-back letter of credit had been honored after the negotiating bank had acquired notice of the fraud. *See* discussion and accompanying text, *supra* notes 223-225 (discussing back-to-back letters of credit).

254. *See* Banque de l'Indochine v. J.H. Ranyner (Mincing Lane), Ltd., [1983] 1 Lloyd's Rep. 228, 230, 234 (C.A. 1982) (stating that "under reserve" meant that, if the issuing bank refused to reimburse the confirming bank due to documentary discrepancies, the beneficiary would repay the confirming bank upon demand and then sue the confirming bank to establish the conformity of the documents). Taking required documents "with recourse" is the same thing as taking them "with reserve." *See* Bright Resources Dev., Ltd. v. Union Bank, CACV 241/1998 [1999] H.K. C.A., ¶ 13, *available at* http://legalref.judiciary.gov.hk/lrs/common/ju/judgment.jsp (last visited Nov. 18, 2008) (describing a deposit as "proceeds of negotiation of a bill with recourse to you"). Another variation is an express warranty by the beneficiary that the documents negotiated conform to the requirements of the letter of credit. *See* Donald Smith, *Negotiation Is Not Always What Bankers Think It Is*, 12 No. 3 DC INSIGHT 9, 10 (July/Sept. 2006) (noting that some negotiation agreements contain a warranty by the beneficiary that the documents conform to the credit in all respects). If a draft in negotiable form is one of the

Due to the inconsistency of a right of recourse with an obligation to negotiate, a confirmer that is obligated to negotiate can not create a right of recourse against the beneficiary.[255] However, nominated negotiating banks that neither are confirmers nor specifically have undertaken to negotiate are merely authorized, not obligated, to negotiate.[256] These negotiating banks are free to require a refund from the beneficiary in the event that reimbursement is denied by the issuer or a confirmer.[257]

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required documents, the beneficiary's signing the draft as drawer or indorser gives a negotiating bank recourse under negotiable instruments law against the beneficiary in the event of dishonor of the draft. *See* U.C.C. §3-414(b)(i) (describing obligation of drawer of draft); U.C.C. § 3-415(a)(i) (describing obligation of indorser). Both a drawer's and an indorser's negotiable instruments law obligation can be disclaimed by the addition of "without recourse" or the equivalent to their signatures. *See* U.C.C. § 3-414(e) (explaining drawer's obligation disclaimable on a draft that is not a check); U.C.C. § 3-415(b) (explaining indorser's obligation disclaimable on any instrument). Sometimes the phrase "under reserve" is used to refer to taking required documents without giving the beneficiary withdrawable credit. *See, e.g.*, DOLAN TREATISE, *supra* note 12, at 8-14 ("Negotiating banks that take the beneficiary's documents under reserve, that is, under an arrangement whereby the beneficiary does not receive credit against which it may draw . . . ."). This type of "under reserve" transaction does not involve UCP 600 negotiation. *See* UCP 600, *supra* note 7, art. 2 (explaining that negotiation requires purchase of required documents with either advance or a promise to make future advance that is performed).

255. UCP 600, *supra* note 7, art. 8(a)(ii) (explaining that a confirming bank must negotiate without recourse).

256. *Id.* art. 12(a) (authorization of a nonconfirming bank to negotiate does not create an obligation to do so).

257. *See* COMPARISON OF UCP 600 & UCP 500, *supra* note 113, cmt. 11, at 36 (explaining that a nominated bank that is not a confirmer negotiates with a right of recourse unless it agrees otherwise). In the interest of finality of payment, confirming banks are required to negotiate drafts drawn upon by other banks and documents without recourse; UCP 600, *supra* note 7, art. 8 (a)(ii) (explaining that a confirming bank undertakes to negotiate, without recourse, if the credit is available by negotiation with the confirming bank). If *Banque de l'Indochine*, [1983] 1 Lloyd's Rep. 228, had arisen under UPC 600, the confirming bank's "under reserve" recourse agreement with the beneficiary would have been unenforceable. On the other hand, a negotiating bank merely giving a beneficiary revocable provisional credit for the required documents does not involve the "advancement of funds" required by the definition of negotiation. *Cf.* U.C.C. §§ 4-210(a)(1), (2) (stating that for a collecting bank to have a statutory security interest in a deposited item provisional credit must have been either withdrawn or available for withdrawal as of right). Professor Dolan had advanced a theory under UCP 500 that negotiating banks could not negotiate with recourse. *See* Dolan, *supra* note 1, at 423-426 (contending that the UCP 500 requirement that an issuer negotiate without recourse applies to a negotiating bank nominated by the issuer). However, UCP 600 has deleted the UCP 500 language upon which Professor Dolan had relied and he has acknowledged that nothing in UCP 600 requires a nominated negotiating bank to negotiate without recourse. *See* John Dolan, *Negotiation Credits Under UCP 600*, 13 No. 1 DC INSIGHT 4 (Jan./Mar. 2007) (positing that the absence of the "without recourse" language in the UCP 600 definition of negotiation and its presence in a confirmer's obligation are strong indications that a nominated negotiating bank can negotiate with recourse).

Negotiation with recourse reallocates the consequences of dishonor. If the issuer or a confirmer dishonors for any reason and a nominated negotiating bank, that has negotiated with recourse, demands a refund from the beneficiary rather than asserting its rights against the issuer or the confirmer, the burden of litigation is shifted to the beneficiary.[258]

3. Implied Authorization for Nominated Banks to Prepay and to Purchase Their Own Accepted Drafts or Deferred Payment Obligations Prior to Maturity—a Side Issue

Article 12(b) of UPC 600 provides that: "By nominating a bank to accept a draft or incur a deferred payment undertaking, an issuing bank[259] authorizes that nominated bank to prepay or purchase a draft accepted or a deferred payment obligation incurred by that nominated bank."[260]

Article 12(b) addresses issues raised by the decision of the United Kingdom Court of Appeal in *Banco Santander v. Bayfern, Ltd.*[261] On June 5, 1998, Banque Paribas issued a $20,315,796.30 deferred payment letter of credit subject to UCP 500 designating Bayfern, Ltd. as beneficiary.[262] The deferred payment was due on November 21, 1998, 180 days after the date of the bill of lading.[263] Santander confirmed the letter of credit on June 8, 1998 and Paribas undertook to reimburse Santander at maturity.[264]

On June 15, 1998, Bayfern presented conforming documents to Santander, which acknowledged its obligation to pay Bayfern the amount of the letter of credit upon November 27, 1998.[265] On June 16, 1998,

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258. *See, e.g.*, GNT Oil Co. v. Hana Bank, HCCL 32/2004 [2005]H.K. C.F.I., ¶¶ 18, 62, 63, *available at* http://legalref.judiciary.gov.hk/lrs/common/ju/judgment.jsp (last visited Nov. 18, 2008) (allowing the beneficiary to recover for wrongful dishonor after the negotiating bank had exercised its right of recourse against the beneficiary).

259. Although Article 12(b) does not expressly state that a confirming bank also authorizes a nominated bank to prepay or to purchase its own acceptance or deferred payment obligation, this authorization is implied. COMPARISON OF UCP 600 & UCP 500, *supra* note 113, cmt. 11, at 117 (explaining that a confirming bank is a nominated bank that makes an Article 12(b) authorization).

260. UCP 600, *supra* note 7, art. 12(b). Prepayment would discharge the obligation prepaid; whereas purchase would not discharge the obligation purchased. *See* COMPARISON OF UCP600 & UCP500, *supra* note 113, cmt. 13, at 117 (explaining prepayment involves discharge while purchase does not).

261. [2000] 1 All E.R. (Comm.) 776.

262. *Id.* at 777-78.

263. *Id.*

264. *Id.*

265. *Id.* at 778.

Santander purchased its own deferred payment obligation, crediting Bayfern's account with the discounted price of $19,667,238.84 in exchange for Bayfern's request for the discount and the assignment to Santander of Bayfern's rights to the proceeds of the letter of credit.[266]

After forwarding the required documents, Santander was informed by Paribas that one or more of them had been forged.[267] On November 27, 1998, Paribas refused Santander's claim for reimbursement and/or payment of the proceeds of the letter of credit due to fraud by Bayfern.[268] A United Kingdom trial court found Paribus' refusal to have been justified.[269]

Upon the stipulations that Bayfern was guilty of fraud and that both Santander and Paribus had notice of the fraud prior to November 27, 1998,[270] the Court of Appeal dismissed Santander's appeal.[271] As assignee of Bayfern's rights to the proceeds of the letter of credit, Santander had been subject to Paribas' fraud defense against Bayfern.[272] With respect to Santander's claim that it had an independent right to reimbursement as a nominated confirmer, Lord Justice Waller reasoned:

> Ultimately the question to be asked is what precisely the issuing bank has requested the confirming bank to do, and what the issuing bank has promised to do if the confirming bank does what is requested of it. The answer, as it seems to me, is that the issuing bank has requested the confirming bank to give its own undertaking to pay on 27 November 1998, in addition to that of the issuing bank, and has promised to reimburse the confirming bank when it pays on that deferred payment undertaking, i.e. pays $US20,315,796.30 on 27 November 1998. There is no request from Paribas that Santander should discount or give any value for the documents prior to 27 November 1998, and albeit it may not be a breach of mandate for Santander to do so, it is up to Santander whether it does so or not....In my view

266. *Id.*

267. *Banco Santander*, [2000] 1 All E.R. (Comm.) at 778.

268. *Id.*

269. *Id.* at 777 (noting that the trial judge had decided preliminary issues in favor of Paribus).

270. *Id.* at 778 (assuming fraud and notice of the fraud to both Santander and Paribus prior to November 27, 1998).

271. *Id.* at 786 (dismissing appeal).

272. *Id.* at 780-83 (ruling that a defence that was available against assignor should be available against assignee).

> the position is that Santander had no authority to negotiate from Paribas to discount, and did not seek it. It was something that 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, and it is in those circumstances not open to them to claim reimbursement from Paribas.[273]

If the *Santander* case had arisen under Article 5, the result would have been different. There would have been two potentially applicable immunity provisions: the provision immunizing a confirmer that has honored its confirmation in good faith,[274] and the provision immunizing an assignee of a nominated person's deferred payment obligation that took for value and without notice of material fraud after the obligation was incurred.[275] Because the confirmed letter of credit had not obligated Santander to purchase its own deferred payment obligation,[276] the confirmer immunity provision would not have applied.[277] However, the immunity provision for an assignee of a nominated person's deferred payment obligation applies to straight letters of credit like that in the *Santander* case as well as to negotiation letters of credit.[278] Santander paid substantial value to Bayfern for Santander's own deferred payment

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273. *Banco Santander*, [2000] 1 All E.R. (Comm.) at 785-86. In *Credit Lyonnais v. Canara Bank Int'l Division*, the French Court of Cassation reached a similar result with respect to a confirming bank that discounted its own accepted time drafts without explicit authorization from the issuer and acquired notice of beneficiary fraud prior to the maturity of the drafts. *See* Georges Affaki, *French Supreme Court on Discounting L/C Acceptances*, 12 No. 2 DC INSIGHT at 11-13 (Apr./June 2006).

274. *See* U.C.C. § 5-109(a)(1)(ii) (explaining that the issuer shall honor a presentation by a confirmer that has honored its confirmation in good faith).

275. *See* U.C.C. § 5-109(a)(1)(iv) (explaining that the issuer shall honor a presentation by an assignee of a nominated person's deferred payment obligation that took in good faith and without notice of forgery or material fraud after the obligation was incurred by the nominated person). A confirmer like Santander must be a nominated person under Article 5. *See* U.C.C. § 5-102(a) (4) ("'Confirmer' means a nominated person . . . .").

276. *Banco Santander*, [2000] 1 All E.R. (Comm.) at 785 (noting that there had been no request by Paribas for Santander to give value before November 11, 1998).

277. *See* U.C.C. § 5-109(a)(1)(ii) (explaining that to be immune a confirmer must have honored its confirmation in good faith). *But see* James G. Barnes, *A US view: US Codified Law is Superior to English Judge-Made Law On the Fraud Exception to the Independence of Letters of Credit*, 6 No. 3 DC INSIGHT 7, 8 (July/Sept. 2000) (positing that U.S. law would have treated Santander as a confirming bank that honoured its confirmation).

278. *See* U.C.C. § 5-109(a)(1)(iv) (stating that immunity is conferred if the assignor was a nominated person and the assignee took in good faith "for value and without notice of forgery or material fraud").

obligation before Paribas had given notice of material fraud and would have been entitled to Article 5 immunity.[279]

In reaction to the *Santander* decision, UCP 600 Article 12(b) deems the nomination of a bank to accept a time draft or to incur a deferred payment obligation to include authorization either to prepay or to purchase[280] the time draft that the nominated bank accepted or the deferred payment obligation that the nominated bank incurred.[281] This implied authorization would estop the issuer, a confirmer, and the applicant from asserting a material letter-of-credit fraud defense against the obligation to reimburse the nominated bank, provided that the bank relied upon the authorization in acquiring its own obligation in good faith and without notice of material fraud.[282] The UCP 600 statement of the undertakings by issuing and confirming banks compliments Article 12(b) by providing that reimbursement for a complying presentation is not due to a nominated bank that has prepaid or purchased its own accepted time draft or deferred payment obligation until the time draft or deferred payment obligation is mature.[283]

Article 12(b) interacts with Section 5-109(a)(1)(i) of Article 5 by increasing the scope of a nomination to accept a time draft and to incur a deferred payment obligation. But, like the UCP 600 definition of negotiation,[284] Article 12(b) does not address the good faith and without

279. *See Banco Santander*, [2000] 1 All E.R. (Comm) at 778 (explaining that Santander purchased its own deferred payment obligation by June 16, 1998 and Paribas did not give notice of fraud until June 24, 1998).

280. Whatever the form of acquiring its own executory obligation, a nominated bank would want to pay less than its face amount and to keep the obligation alive in order to obtain full reimbursement upon the maturity date. Thus in *Banco Santander*, Santander advanced $19,667,238.84 for its $20,315,796.30 deferred payment obligation and had taken an assignment of Bayfern's right to the proceeds of the letter of credit. Professor Byrne takes the position that a nominated bank's prepayment of its own deferred payment obligation necessarily would discharge that obligation. *See* COMPARISON OF UCP600 & UCP500, *supra* note 113, cmt. 13, at 117 ("[P]repay refers to discharge of one's own obligation . . . ."). To the extent that this is so, nominated banks would prefer to purchase their own deferred payment obligations. *See id.*

281. *See* UCP 600, *supra* note 7, art. 12(b).

282. See *European Asian Bank*, [1983] 1 Lloyd's Rep. at 619-20 (ruling that the issuer had been estopped to deny its obligation to reimburse a bank that had negotiated the required documents following that bank's prejudicial reliance upon the issuer's representation that reimbursement would be forthcoming). Professor Byrne believes that "UCP 600 makes it clear that the nominated bank is entitled to be reimbursed notwithstanding beneficiary letter of credit fraud." COMPARISON OF UCP600 & UCP500, *supra* note 113, cmt. 12, at 117.

283. UCP 600, *supra* note 7, arts. 7(c), 8(c) (stating that reimbursement is due "at maturity").

284. UCP 600, *supra* note 7, art. 2. *See* discussion and accompanying text, *supra* note 251.

notice of material fraud conditions of nominated bank immunity. If a nominated bank had given value by prepaying or purchasing a time draft that it had accepted or a deferred payment obligation that it had incurred with knowledge or notice of material fraud, the nominated bank would be subject to remedies for that fraud.[285]

Issuing banks and applicants can react to Article 12(b) in several ways. In order to avoid increasing nominated bank immunity from remedies for material fraud, Art. 12(b) could be excluded from the incorporation of UCP 600 into a letter of credit[286] or UCP 500, which had no counterpart of Article 12(b), could be incorporated instead of UCP 600.[287] Issuers that do not exclude Article 12(b) must ensure that their reimbursement agreements with applicants unambiguously cover the reimbursement of a nominated bank that has prepaid or purchased its own acceptance or deferred payment obligation in good faith and without notice of material fraud.[288]

But, whatever its fate in the marketplace, Article 12(b) does not cover banks exclusively nominated to negotiate. For Article 12(b) to

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285. *See* U.C.C. § 5-109(a)(1)(i); discussion and accompanying text, *supra* notes 251-253.

286. There is authority for the proposition that an express provision in a letter of credit incorporating the UCP that is inconsistent with a UCP provision impliedly overrides the UCP provision. *See, e.g.*, Korea Exchange Bank v. Standard Chartered Bank, [2006] 1 S.L.R. 565, 575-79 (Sing. H.C. 2006) (ruling that two express provisions in the letter of credit negated the UCP 500 provision that nondocumentary provisions are to be disregarded). Nevertheless, express negation of UCP provisions intended to be excluded from incorporation is the prudent course.

287. UCP 600 only applies to the extent that the text of a letter of credit expressly indicates that the letter of credit is subject to UCP 600. UCP 600, *supra* note 7, art. 1 (stating that UCP 600 applies "when the text of the credit expressly indicates that it is subject to these rules . . . [the UCP 600 rules can be] expressly modified or excluded by the credit"); COMPARISON OF UCP 600 & UCP 500, *supra* note 113, at 5 (advising issuers to "[g]ive careful thought to provisions of UCP600 that should be varied"). *See* John F. Dolan, *Discounting Deferred Payment Obligations*, 11 No. 4 DC INSIGHT 8, 9 (Oct./Dec. 2005) (contending that banks and commercial parties that prefer the protection against beneficiary fraud afforded by the *Banco Santander* approach will be inclined to avoid UCP 600 Article12(b)). A letter of letter credit providing for delayed payment enables the applicant to inspect the goods prior to payment and to discover any beneficiary fraud. *See* discussion and accompanying text, *supra* notes 68-69.

288. *See* Mohammad Burjaq, *A Reaction from the Middle East*, 13 No. 1 DC INSIGHT 9, 10 (Jan./Mar. 2007) (noting that Middle Eastern commentators believe that Article 12(b) gives rise to a real risk to the issuing bank and that one solution would be to exclude Article 12(b) from the incorporation of UCP 600 and to require a prior authorization for the discount of acceptances and deferred payment obligations. Another solution would be to add an express provision to the applicant's reimbursement agreement in which the applicant agrees to reimburse a discounted payment even if beneficiary fraud is discovered before the maturity of the acceptance or the deferred payment obligation).

apply, a bank previously must have acted upon the nomination to accept a time draft or to incur a deferred payment obligation without knowledge or notice of material fraud.[289] Merely acting upon the nomination to purchase the required documents does not invoke Article 12(b).[290]

VII. CONCLUSION

UCP 600 clarifies the concept of negotiation by requiring the purchase of the required documents by a nominated negotiating bank, either by advancing funds or by agreeing to advance funds as directed by the beneficiary and subsequently making the advance.[291] Funds are advanced "to" the beneficiary when the funds are disbursed in accordance with the beneficiary's instructions. The actual payments can be to third parties.[292]

The banking day upon which reimbursement is due to a nominated negotiating bank that has negotiated and forwarded the documents is the UCP 600 deadline for performance of an executory promise to make an advance.[293] With respect to letters of credit payable at "sight," reimbursement is due either upon the issuer's or a confirmer's determination that a complying presentation[294] of documents has been made[295] or upon the issuer's or a confirmer's preclusion to deny the existence of a complying presentation due to failure to give effective

289. *See* UCP 600, *supra* note 7, art. 2 (explaining that negotiation is the purchase of documents).

290. *See id.* art. 12(b) (stating the limitation to banks nominated to accept drafts and to incur deferred payment obligations).

291. *See id.* art. 2; DRAFTING GROUP COMMENTARY UCP 600, *supra* note 7, at 22 ("UCP 600 has changed and simplified the definition to focus the concept on the purchase of drafts and/or documents by advancing, or agreeing to advance, funds to the beneficiary on or prior to the banking day that reimbursement is due."). The issuing bank and a confirming bank are obligated to reimburse a nominated negotiating bank that has negotiated and forwarded the documents upon the "maturity" of the issuing or the confirming bank's obligation under the letter of credit. *See* UPC 600, *supra* note 7, arts. 7(c), 8(c).

292. *See* discussion and accompanying text, *supra* notes 221-222.

293. *See* discussion and accompanying text, *supra* note 214.

294. *See* UCP 600, *supra* note 7, art. 2 (explaining that a complying presentation is in accordance with the terms and conditions of the credit, the applicable provisions of UCP 600, and international standard banking practice).

295. *See* UCP 600, *supra* note 7, arts. 15(a), 15(b) (explaining that, if the issuing bank determines that a presentation is complying, it must honour; if a confirming bank determines that a presentation is complying, it must honour or negotiate as the case may be); arts. 7(c), 8(c) (obligating the issuing bank or a confirming bank to reimburse a negotiating bank that has acted upon its nomination and forwarded the documents upon the "maturity" of the issuing or confirming bank's obligation to honour).

notice of refusal of the documents.[296] With respect to letters of credit available by acceptance or by a deferred payment obligation, reimbursement is due upon the maturity of the accepted time draft or the maturity of the deferred payment obligation.[297]

Subject to the deadline of the banking day upon which reimbursement is due, both the amount and the timing of a nominated negotiating bank's advance are left to the parties.[298] However, negotiation does not occur until the promised purchase price has been advanced. A promise to advance the purchase price to a fraudulent beneficiary does not confer immunity from letter-of-credit fraud prior to its performance.[299]

The UCP 600 Drafting Group has not commented upon the significance of the new definition of negotiation for the purchase of the required documents in exchange for the satisfaction or the securing of an antecedent debt.[300] Nevertheless, the UCP 600 requirement that *funds be advanced*[301] implicitly rejects including satisfaction of a truly antecedent debt of the beneficiary to the negotiating bank or the securing of a truly antecedent debt of the negotiating bank to the beneficiary as all or part of the price for the documents. On the other hand, a contemporaneous advance in anticipation of negotiation of the required documents should satisfy the definition of negotiation. In *Nanyang Commercial Bank v. Man Sam Kwan*,[302] for example, the issuer of a back-to-back letter of credit initially recorded the amount paid to the beneficiary of the back-to-back letter of credit as a debt of the applicant but then credited the applicant with the purchase price of the documents required by the

296. *See* UCP 600, *supra* note 7, arts. 16(c), (d), (f) (explaining that failure of the issuing bank or a confirming bank to give notice of refusal as required by Article 16 precludes the bank from claiming that the documents do not constitute a complying presentation). UCP Articles 7(c) and 8(c) require the issuing bank and a confirming bank to reimburse a negotiating bank that has acted on its nomination and forwarded the documents upon the "maturity" of the issuing bank's or the confirming bank's obligation to honour. UCP 600, *supra* note 7, arts. 7(c), 8(c).

297. *See id.*

298. *See* UCP 600, *supra* note 7, art. 2 (omitting parameters for the amount of the purchase price or the time at which an advance prior to the banking day of reimbursement should be made).

299. *See* discussion and accompanying text, *supra* notes 248-250.

300. *See* UCP 500, *supra* note 7, art. 10(b)(ii) (negotiation is the giving of value for drafts or documents); DOLAN TREATISE, *supra* note 12, at 8-6 (explaining that under the U.C.C., taking for an antecedent debt is "value").

301. *See* UCP 600, *supra* note 7, art. 2 (emphasis added) ("[P]urchase . . . by advancing or agreeing to advance funds to the beneficiary . . . .").

302. HCMP 403/1999 [2006] H.K. C.F.I. *available at* http://legalref.judiciary.gov.hk/-lrs/common/ju/judgement.jsp (last visited Nov. 18, 2008).

primary letter of credit. The court found that negotiation took place under UCP 400.[303]

Precluding a nominated negotiating bank from using the payment or the securing of an antecedent debt to purchase required documents is an undesirable and unnecessary restriction upon negotiation that previously was permissible. It also is unfortunate that the UCP 600 definition of negotiation does not articulate the inherent distinction between the executory negotiation created by a promise to make an advance in the future and the actual negotiation resulting from performance of the executory promise. In order to forestall unnecessary immunity from material letter-of-credit fraud, the courts must draw this distinction. A nominated negotiating bank that acquires notice of material fraud prior to performance of an executory promise to make an advance that has been made to the beneficiary alone, need not be immunized from remedies for the fraud. The negotiating bank can avoid loss by using the fraud to justify nonperformance of its executory obligation.[304] The UCP 600 definition of negotiation otherwise conforms to Article 5 policy with respect to immunity from remedies for material letter-of-credit fraud and exemplifies the ICC tradition of periodic refinement of the UCP.[305]

303. *See id.* ¶¶ 6-29, 43, 56-58. *See* discussion, *supra* notes 223-225 (discussing back-to-back letters of credit).

304. *See* discussion and accompanying text, *supra* note 110.

305. Counting UCP 600, the UCP has been revised six times since 1933. *See* COMPARISON OF UCP 600 & UCP 500, *supra* note 113, at vi, n.1 (explaining that the UCP was revised in 1951, 1962, 1974, 1983, 1993 and 2007).