

Documentary Credit

WORLD

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■ BANK PAYMENT OBLIGATION

The concept of the Bank Payment Obligation was first introduced to the international banking community five years ago and launch of the Uniform Rules for BPO (URBPO) followed in June 2013 to govern practice for this product. The goal of the BPO is to reintroduce banks into the supply chain process from which they have been increasingly excluded by open account transactions. The BPO has been described as an irrevocable and independent undertaking issued by a bank to another bank that payment will be made on a specified date after successful electronic matching of data. While some people have drawn sharp distinctions between BPO and LCs, others have suggested that BPO is the latest attempt to electrify the commercial letter of credit. In this issue, Matthew V. Raketti delves into this area.

Foreign Venture Limited Partnership v. Chemical Bank 59 A.D.2d 352 (N.Y. App. Div. 1977) [USA]

Topics: Preliminary Injunction; Preferential Payment; Bankruptcy; UCP 222 Article 8; UCP600 Article 5 (Documents v. Goods); Prior US UCC § 5-114 (Issuer's Duty and Privilege to Honor; Right to Reimbursement); [current US UCC Section 5-109 (Fraud and Forgery)]; Independence; Preference; Fraud Exception; Applicant Not Party

Type of Lawsuit: Applicant Partnership sued Issuer and Beneficiary/Lender to enjoin payments under standby letters of credit.

Parties: Respondent/Plaintiff/Applicant/Partnership– Foreign Venture Limited Partnership. (Counsel: David C. L. Frauman of counsel- John J. Jerome with him on the brief; Milbank, Tweed, Hadley & McCloy, attorneys.)

Appellant/Defendant/Issuer– Chemical Bank (Counsel: John G. Koeltl of counsel (Ralph L. McAfee, Richard S. Simmons, David O. Brownwood, Steven C. Schroer and Robert B. von Mehren with him on the brief; Cravath, Swaine & Moore and Debevoise, Plimpton, Lyons & Gates, attorneys)

Appellant/Defendant/Beneficiary/Lender– Commercial Banking Company of Sydney, Ltd. (Counsel: John G. Koeltl of counsel (Ralph L. McAfee, Richard S. Simmons, David O. Brownwood, Steven C. Schroer and Robert B. von Mehren with him on the brief; Cravath, Swaine & Moore and Debevoise, Plimpton, Lyons & Gates, attorneys)

Australian Affiliate– Venture Carpets PTY., Ltd.

Underlying Transaction:

Loan by Australian Bank to Australian Affiliate.

LC: Two irrevocable standby LCs totaling USD 480,000. Subject to UCP 222 (1962).

Decision: The Supreme Court of New York (trial court), Nadel, J., partially enjoined payment on the standby. On appeal, the Supreme Court of New York, Appellate Division, Silverman, J., (1) reversed the decision of the trial court, (2) dismissed the Plaintiff's complaint, and (3) vacated the preliminary injunction.



"An Oldie But a Goodie"

Rationale: Irrevocable letters of credit must be honored without regard to the underlying transaction absent any fraud. In addition, failure of the beneficiary to credit its receipt of an invalid preferential payment against the debt covered by the letters of credit does not constitute fraud in a transaction. Applicant/Partnership had no right to interfere with the honoring of the letters of credit.

What This Case Means for LC Specialists Today:

Although decided under the 1962 revision of the UCP and the prior revision of the US UCC Article 5 (Letter of Credit), the principles stated in this decision remain valid. A dispute regarding the preference funds paid is not the type of fraud that would warrant injunctive relief without more. A complying presentation must be honored unless there is serious fraud disrupting the underlying transaction completely.

Factual Summary:

To assure repayment of a loan to its Australian Affiliate, Partnership caused Chemical Bank (Issuer) to issue two standby letters of credit in favor of Commercial Banking Company of Sydney (Beneficiary/Lender). The standby stated that it was available, “against your [Beneficiary] request stating that the liability or any part thereof by [Australian Affiliate] to yourselves remains unpaid at maturity and that your drawing on this credit covers the portion which remains unpaid.” When the Australian Affiliate experienced financial difficulties, Applicant/Partnership liquidated its assets, paying Beneficiary/Lender and reducing the debt to AUD 135,717. Subsequently, a bankruptcy liquidator was appointed who demanded the funds deposited, causing Beneficiary/Lender to debit the Affiliate’s account and to draw on the standbys.

Applicant/Partnership sued Issuer and Beneficiary/Lender to enjoin honor or receipt of payment. A preliminary injunction was granted. On appeal, the court reversed the preliminary injunction and remanded the case.

Legal Analysis:

1. Independence; Preference: The Applicant/Partnership argued that under Australian Law, the payment had operated to reduce the indebtedness to Beneficiary/Lender, which could not be reinstated because it was subsequently determined to be preferential. The Judge rejected this claim, referring to UCP 222 (1962) Article 8 for the proposition that “In documentary credit operations all parties concerned deal in documents and not in goods”. The Judge also referred to Prior UCC Section 5-114 which provided that “(1) An issuer must honor a draft or demand for payment which complies with the terms of the relevant credit regardless of whether the goods or documents conform to the underlying contract for sale or other contract between the customer and the beneficiary.” The Judge ruled that “if the documents are in good form, as they are here, that is in general the end of the inquiry as to the right of the drawee bank to honor drafts drawn against the letters of credit”.

2. Fraud Exception: The Judge noted that the exception of the “narrow exception” where there is fraud in the transaction under Prior UCC Section 5-114(2). He then stated that the “rather subtle dispute” about preferential payment “is surely not fraud in the transaction.” The Judge also noted

that equitable consideration regarding injunctions would favor its denial since the bank's agent whom claim were made were solvent and available in the forum.

3. Applicant Not Party: The Judge noted that because the Partnership/Applicant is a party to a separate contract than the LC, then it is not a party. ■

[TR]



NEWLY DECIDED LC & GUARANTEE CASES

Alessandra Yarns, L.L.C. v. Tongxiang Baoding Textile Co.
2015 QCCS 346 [Canada]

Ask Re Ltd v. Grain Mineral Resources Pte Ltd
[2015] HKCU 1639 [Hong Kong]

Calm Ocean Shipping SA v. Win Goal Trading Ltd
[2015] HKEC 2283 [Hong Kong]

Caterpillar Motoren GmbH & Co. K.G. v. Mutual Benefits Assurance Company
[2015] EWHC 2304 (Comm) [England]

Fabtech Australia Pty Ltd v. Laing O'Rourke Australia Construction Pty Ltd
[2015] FCA 1371 [Australia]

Jabneel Development Inc. v. Lamont
[2015] A.J. No. 847, 2015 ABQB 488 [Canada]

People v. Tirey
No. G048369 (Cal. Ct. App. Nov. 10, 2015) [USA]

Transerve Pte Ltd v. Blue Ridge WA Pty Ltd.
[2015] FCA 953 (2015) [Australia]

Yuanda Australia Pty Ltd v. John Holland Pty Ltd
[2015] WASC 453 (2015) [Australia]

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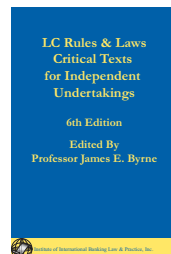
REFERENCE MATERIALS

The Institute offers the most comprehensive collection of reference materials in the industry. It also regularly conducts seminars on topical issues, general educational forums, and custom training for bankers, lawyers and corporate financiers. All of these products are designed to assist the letter of credit professional with the practical issues you face on a daily basis. Its newest and most popular reference materials include:



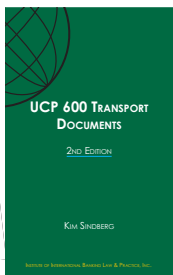
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2016 EDUCATIONAL CALENDAR

*The World's
Premiere LC Event of the Year!*

*World's Only Event
for Interactive Discussion
of Guarantee & Standby Topics*

*Full Day Focus on LC Practice,
Forms, and Litigation Issues*

Annual Survey of Letter of Credit Law & Practice

AMERICAS: Tampa – 17-18 March 2016
MIDDLE EAST: Dubai – 3-4 Apr 2016
EUROPE: Stockholm – 23 May 2016
EUROPE: Utrecht – 27 May 2016
HONG KONG: 9 July 2016
SE ASIA: Singapore – 11-12 July 2016
CHINA: Shanghai – 16-17 July 2016

Guarantee & Standby Forum

EUROPE: Stockholm – 24 May 2016
EUROPE: Utrecht – 26 May 2016
HONG KONG: 8 July 2016
SE ASIA: Singapore – 13 July 2016
CHINA: Shanghai – 18 July 2016
AMERICAS: New York – October 2016

Letter of Credit Law Summit

SE ASIA: Singapore – 14 July 2016
AMERICAS: New York – October 2016

Other 2016 events, dates, and locations are pending and will be announced. For the most current information, visit: www.iiblp.org For a complete list of resources available, please contact the Institute.

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