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THE DRAFT CONVENTION ON INDEPENDENT GUARANTEES

AND STAND-BY LETTERS OF CREDIT

(VIENNA, MAY 1995)

AND "DEMAND GUARANTEES"(ICC PUB.458)

AND UCP 500 IN RELATION TO STAND-BY CREDITS

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Ladies and Gentlemen,

I am glad to have this opportunity to talk to you and to make some comments on the rules of guarantees from different sources, as such guarantees are always needed by those who implement BOT projects.

"Independent guarantees" is a term almost near to "demand guarantees" regulated by the ICC collection No. 458 issued in 1992. "Stand-by letters of credit" are also regulated by the UCP 500 issued in 1993. The sets of rules of the ICC take their force from the agreement of parties upon them, where the parties refer to one of these sets it applies. But the new Uncitral Rules are intended to be either a model law, or to be a draft convention. In case they become a Convention they will have the force of law and be applied unless excluded.

Stand-by L/Cs differ from demand guarantees in that they have a wider scope of application as they may relate to financial obligations as well as non financial obligations. Demand guarantees relate always to financial obligations. Stand-by L/Cs may be confirmed, while in demand

guarantees it is not current to confirm them. Stand-by may be paid at the counters of a bank other than the issuing bank, and this does not occur in demand guarantees. Stand-by may be used to guarantee the commitments of the issuing bank itself, but this idea is excluded from the sphere of demand guarantees which must be issued upon instructions from a principal or an instructing party.

In May 1995 the UNCITRAL has launched a draft of new collection of rules for independent guarantees, stand-by letters of credit, but do not cover indemnities (Guarantees are issued to secure the default of the debtor; whereas indemnities secure the loss caused by the debtor to the creditor. See: Lars Gorton, Lloyd's Maritime and Commercial Law Quarterly, 1996, Part 1, February 1996, p. 42).

We shall give herebelow some comments and remarks on the said draft convention containing the Uncitral Rules compared with the provisions of demand guarantees (Publication No.458 of the ICC).

1. It is noted the influence of the anglosaxon legal concepts in the draft convention such as article 14 (gross negligent conduct), article 19 (willful misconduct) and article 12 (the limitation of six years).

2. As a whole the relevant sets of rules of the ICC tend to simplify and to consecrate practice, while the draft convention. tends to be concise to the extent that it seems for the first reading to be complicated.

3. When the new Convention enters into force among member States it will apply to international independent guarantees and stand-by letters of credit automatically,

unless its application is excluded in the undertaking. If the Uncitral Rules are not excluded they will apply even where no reference is made to them. Article 1 of the draft Convention relating to the scope of application says:

"1. This Convention applies to an international undertaking referred to in article 2:

"a) If the place of business of the guarantor/issuer at which the undertaking is issued is in a Contracting State; or

"b) If the rules of private international law lead to the application of the law of a Contracting State, unless the undertaking excludes the application of the Convention.

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

"3. The provisions of articles 21 and 22 (relating to the applicable law) apply to international undertakings referred to in article 2 independently of paragraph 1 of this article."

4. The draft Convention includes international letters of credit not falling within the undertakings covered by the Convention, if they expressly state that they are subject to the Convention.

5. Local independent guarantees and stand by letters of credit are subject to the provisions of the national laws and not to the provisions of the Convention. Such local undertakings may follow the provisions of the Convention and in such case the Convention enters the national law by imitation in certain cases. The rules of Demand Guarantees (publication 458 of the ICC) apply to

international as well as to local guarantees where the said publication is expressly mentioned in the guarantee.

6. Article 2 of the draft Convention stipulates that:

"1. For the purposes of this Convention, an undertaking is an independent commitment, known in international practice as an independent guarantee or as a stand by letter of credit, given by a bank or other institution or person ("guarantor/issuer") to pay to the beneficiary a certain or determinable amount upon simple demand or upon demand accompanied by other documents in conformity with the terms and any documentary conditions of the undertaking, indicating, or from which it is to be inferred, that payment is due because of a default in the performance of an obligation, or because of another contingency, or for money borrowed or advanced, or on account of any mature indebtedness undertaken by the principal/applicant or another person.

"2. The undertaking may be given:

"(a) At the request or on the instruction of the customer ("principal/applicant") of the guarantor/issuer.

"(b) On the instruction of another bank, institution or person ("instructing party") that acts at the request of the customer ("principal/applicant") of that instructing party; or

"(c) On behalf of the guarantor/issuer itself.

"3. Payment may be stipulated in the undertaking to be made in any form, including:

"(a)Payment in a specified currency or unit account;

"(b) Acceptance of a bill of exchange (draft);

"(c) Payment on a deferred basis;

"(d) Supply of a specified item of value.

"4. The undertaking may stipulate that the guarantor/issuer itself is the beneficiary when acting in favour of another person."

The draft Convention is not confined to the independent guarantees and stand by letters of credit known in banking practice, but extends to include such undertakings where issued by any "institution" or "person". This may include civil as well as commercial guarantees even given by individuals who may not be aware of the meaning of a stand by letter of credit. The Convention may comprise the positions of : the surety of a debtor in a civil debt, the guarantor of a guarantor (certificateur in French), the partner who guarantees his company, if such obligations were independent from the underlying relationships. It may also comprise insurance policies issued in favor of third parties in international transactions.

The guarantor/issuer may undertake on behalf of the applicant, or on his own behalf, that is to say that the guarantor/issuer guarantees himself viz a viz the beneficiary (Article 2.2.c of the draft Convention). In this way the scope of application of the Convention will not be limited to the independent guarantees and stand by letters of credit, but may extend to personal undertakings emanating from any debtor in a civil or commercial relationship. The rules of demand guarantees of the ICC do not cover the case in which the guarantor guarantees himself.

The limited number of articles in the convention is not enough to cover this wide range of bilateral and unilateral undertakings provided for, and recourse to the applicable law is inevitable.

It is, also, well known that merger in ownership ("la confusion" in French) is a way of extinction of obligations. Meanwhile article 2.4 of the Convention makes such obligation survive if the guarantor/issuer is acting on behalf of another person. This solution is a good practical trend.

7. The stand-by credit is not defined in the draft convention and is sometimes misunderstood in practice. According to the ICC:"Stand by credits are considered to be the secondary means of payment, and therefore such credits should be issued available only against a certificate of default and should not be accompanied by any copies of the commercial documents". (See: Documentary credits insight: ICC Publication, vol. 1 no. 4, Autumn 1995, p. 13).

8. Article 3 relating to the Independence of the undertaking, provides that:

"For the purposes of this Convention, an undertaking is independent when the guarantor/issuer's obligation to the beneficiary is not:

"(a) Dependent upon the existence or validity of any underlying transaction, or upon any other undertaking (including stand by letters of credit or independent guarantees to which confirmations or counter guarantees relate); or

"(b) Subject to any term or condition not appearing in the undertaking or to any future, uncertain act or event except presentation of documents or another such act or event within a guarantor/issuer's sphere of operations".

The independent undertaking or "l'obligation abstraite" in French is met in this article as well as in article 3 of the UCP 500 and in article 3 of the uniform rules for demand guarantees.

9. Article 4 relating to the internationality of undertaking stipulates that:

"1. An undertaking is international if the places of business, as specified in the undertaking, of any two of the following persons are in different States: guarantor/issuer, beneficiary, principal/applicant, instructing party, confirmer.

"2. For the purposes of the preceding paragraph:

"(a) If the undertaking lists more than one place of business for a given person, the relevant place of business is that which has the closest relationship to the undertaking;

"(b) If the undertaking does not specify a place of business for a given person but specifies its habitual residence, that residence is relevant for determining the international character of the undertaking".

An undertaking is international in the following cases if any two of the following places exist in two different States:

i) the places of business of the guarantor/issuer and the beneficiary;

ii) the places of business of the guarantor/issuer and the principal/applicant;

iii) the places of the guarantor/issuer and the instructing party;

iv) the places of the guarantor/issuer and the confirmer;

v) the places of the beneficiary and the principal/applicant;

vi) the places of the beneficiary and the confirmer;

vii) the places of the beneficiary and the instructing party;

viii) the places of the principal/applicant and the instructing party;

ix) the places of the confirmer and the principal/applicant;

x) the places of the confirmer and the instructing party.

The international character of the undertaking ensues that it will be subject to the provisions of the Convention. Meanwhile, a domestic undertaking may provide for the applicability of the Convention and in such case we believe that such undertaking will be subject to the provisions of the Convention, unless such provisions contradict an imperative rule in the relevant national law. ICC uniform rules for demand guarantees did not deal with the international character of an undertaking because they were meant to govern international as well as domestic guarantees.

10. The draft Convention contained a chapter for interpretation (Articles 5 & 6). According to Article 5:

"In the interpretation of this Convention, regard is to be had to its international character and to the need to promote uniformity in its application and the observance of good faith in the international practice of independent guarantees and stand by letters of credit".

Indeed, it is very difficult to realize uniformity in the application of the Convention, as the means of interpretation differ in romano- germanic countries from those in anglosaxon countries. To maintain uniformity judges in different countries should be able to peruse legal decisions of courts in other countries to see how they interprete the Convention. Although such decisions are published, it is not possible to charge a judge to know what is going on in countries other than his.

11. Article 6 puts some definitions:

"For the purposes of this Convention and unless otherwise indicated in a provision of this Convention or required by the context:

"(a) "Undertaking" includes "counter guarantee" and "confirmation of an undertaking";

"(b) "Guarantor/issuer" includes "counter guarantor" and "confirmer";

"(c)"Counter guarantee" means an undertaking given to the guarantor/issuer of another undertaking by its instructing party and providing for payment upon simple demand or upon demand accompanied by other documents, in conformity with the terms and any documentary conditions of the undertaking, indicating, or from which it is to be inferred, that payment under that

other undertaking has been demanded from or made by, the person issuing that other undertaking;

"(d) "Counter guarantor" means the person issuing a counter guarantee;

"(e) "Confirmation" of an undertaking means an undertaking added to that of the guarantor/issuer, and authorized by the guarantor/issuer, providing the beneficiary with the option of demanding payment from the confirmer instead of from the guarantor/issuer, upon simple demand or upon demand accompanied by other documents, in conformity with the terms and any documentary conditions of the confirmed undertaking, without prejudice to the beneficiary's right to demand payment from the guarantor/issuer;

"(f) "Confirmer" means the person adding a confirmation to an undertaking;

"(g) "Document" means a communication made in a form that provides a complete record thereof".

Confirmation may be added to the undertakings according to the Uncitral Rules; but it was not in mind at the time of issuing the uniform rules for demand guarantees of the ICC.

12. Article 7 relating to issuance and irrevocability of undertaking stipulates in paragraph 1 that: "Issuance of an undertaking occurs when and where the undertaking leaves the sphere of control of the guarantor/issuer concerned".

This provision is very important because Article 9/d/ii of the UCP 500 contained a provision to the effect that the commitment begins (in cases of amending a credit or a

stand-by credit) from the time of issuance, but it did not contain what is meant by issuance. This led to a controversy in this matter. Here, Article 7/1 interpretes issuance to mean leaving the sphere of control of the guarantor/issuer. Thus issuance may be completed at the place and time where the undertaking is delivered at the place of business of the beneficiary or in his post box, because before this event the guarantor/issuer can, theoretically, restitute his undertaking, being under his control.

13. Paragraph 2 of Article 7 stipulates that:

"An undertaking may be issued in any form which preserves a complete record of the text of the undertaking and provides authentication of its source by generally accepted means or by a procedure agreed upon by the guarantor/issuer and the beneficiary".

This paragraph is referred to by several subsequent articles. But it must be noted that any agreement between the guarantor/issuer and the beneficiary must not be harmful to the rights of the principal/applicant or the account party, otherwise it will be inoperative. It was better to make the Convention more clear on this point.

The form and contents of an undertaking are usually discussed first between the beneficiary and the applicant/principal; and the form referred to in Article 7/2 is not practical as it rarely occurs that the beneficiary goes in contact with the guarantor/issuer without the intervention of the principal/applicant.

Authentication is realised by signatures or, as a substitute, by cipher codes or swift, but we must note that a credit or stand by letter of credit transmitted by swift without

reference to the UCP 500 shall notwithstanding be subject to the said UCP 500, and in such case the Convention may tacitly lose its applicability.

14. Article 7 contains two other paragraphs as follows:

"(3) From the time of issuance of an undertaking, a demand for payment may be made in accordance with the terms and conditions of the undertaking, unless the undertaking stipulates a different time.

"(4) An undertaking is irrevocable upon issuance, unless it stipulates that it is revocable".

The last paragraph is equivalent to Article 6/c of the UCP 500 and contrary to article 7 of the UCP 400. Indeed, the ICC was codifying the practice since 1933 and thus mentioned always the revocability of credits unless otherwise stated in the credit, but in the UCP 500 it began to try to guide the practice in this issue and the Convention followed it imposing the irrevocability of credits and undertakings. Irrevocability appears also in the uniform rules for demand guarantees of the ICC, Article 5.

15. Article 8 relating to amendments provides that :

"1. An undertaking may not be amended except in the form stipulated in the undertaking or, failing such stipulation, in a form referred to in paragraph 2 of Article 7.

"2. Unless otherwise stipulated in the undertaking or elsewhere agreed by the guarantor/issuer and the beneficiary, an undertaking is amended upon issuance of the amendment if the amendment has previously been authorised by the beneficiary.

"3. Unless otherwise stipulated in the undertaking or elsewhere agreed by the guarantor/issuer and the beneficiary, where any amendment has not previously been authorised by the beneficiary, the undertaking is amended only when the guarantor/issuer receives a notice of acceptance of the amendment by the beneficiary in a form referred to in paragraph 2 of Article 7.

"4. An amendment of an undertaking has no effect on the rights and obligations of the principal/applicant (or an instructing party) or of a confirmer of the undertaking unless such person consents to the amendment".

This rule is similar to that of the UCP 500 contained in Article 9/d/iii thereof. The problem with the two sets of rules is: to what extent is the beneficiary entitled to delay his acceptance to the amendment. In other words, can the beneficiary stay silent till the time of presentation of the claim for payment and choose at that time between the amendment and the original commitment? The UCP answers positively and it seems that the draft Convention is going in the same way as no limitation of the right of the beneficiary in this respect is found in the new rules.

To explain the risks implied in these rules we shall give two examples:

The first example: an undertaking in the form of a stand-by letter of credit for one million Dollars, amended upon instructions from the applicant to be ten million Dollars. The beneficiary keeps silent until the time of shipping, where he seeks his interest as follows: if the prices of the goods raised he ships goods for one million because the rest will be sold at higher prices. If prices went down he ships goods for ten million because he wants to get rid of

his goods at a higher price than the current prices. This causes harm to the applicant but it cannot be cured.

The second example: a stand-by letter of credit issued for goods to be shipped fob from Venice and amended afterwards upon instructions from the applicant to make shipment from Rome. If the beneficiary keeps silent until the time of shipping, he will cause great trouble for the applicant who is required to arrange for the transport from one of these ports and it will be too late for him to provide the required vessel.

The same problem arises where the port of destination is Jeddah on the Red Sea and the amendment made it Dammam on the Gulf. If the beneficiary do not accept the amendment, the applicant will suffer between two ports the distance between them exceeds 1500 km!

Such prejudice to the applicant will not occur if the acceptance of the beneficiary is required before the amendment is issued or if a period of acceptance is stated after which and failing to have any answer, the amendment is considered accepted.

16. Article 9 relating to transfer provides that:

"1. The beneficiary's right to demand payment may be transferred only if authorised in the undertaking, and only to the extent and in the manner authorised in the undertaking.

"2. If an undertaking is designated as transferable without specifying whether or not the consent of the guarantor/issuer or another authorised person is required for the actual transfer, neither the guarantor/issuer nor any other authorised person is obliged to effect the transfer

except to the extent and in the manner expressly consented to by it".

It may be understood from this Article that transfer is always subject to the consent of the guarantor/issuer unless the undertaking states that the transfer does not need such consent. ICC uniform rules for demand guarantees are different as transfer is forbidden but the assignment of proceeds is allowed (Article 4).

17. Article 10 relating to the assignment of proceeds stipulates that:

"1. Unless otherwise stipulated in the undertaking or elsewhere agreed by the guarantor/issuer and the beneficiary, the beneficiary may assign to another person any proceeds to which it may be, or may become, entitled under the undertaking.

"2. If the guarantor/issuer or another person obliged to effect payment has received a notice originating from the beneficiary, in a form referred to in paragraph 2 of Article 7, of the beneficiary's irrevocable assignment, payment to the assignee discharges the obligor, to the extent of its payment, from its liability under the undertaking".

This means that the proceeds of the undertaking are by their nature assignable to third parties, unless the undertaking states otherwise.

18. Article 11 relating to cessation of the right to demand payment says:

"1. The right of the beneficiary to demand payment under the undertaking ceases when:

“(a) The guarantor/issuer has received a statement by the beneficiary of release from liability in a form referred to in paragraph 2 of Article 7;

“(b) The beneficiary and the guarantor/issuer have agreed on the termination of the undertaking in the form stipulated in the undertaking or, failing such stipulation, in a form referred to in paragraph 2 of Article 7;

“(c) The amount available under the undertaking has been paid, unless the undertaking provides for the automatic renewal or for an automatic increase of the amount available or otherwise provides for continuation of the undertaking;

“(d) The validity period of the undertaking expires in accordance with the provisions of Article 12.

“2. The undertaking may stipulate, or the guarantor/issuer and the beneficiary may agree elsewhere, that return of the document embodying the undertaking to the guarantor/issuer, or a procedure functionally equivalent to the return of the document in the case of the issuance of the undertaking in non paper form, is required for the cessation of the right to demand payment, either alone or in conjunction with one of the events referred to in subparagraphs (a) and (b) of paragraph (1) of this Article. However, in no case shall retention of any such document by the beneficiary after right to demand payment ceases in accordance with subparagraph (c) or (d) of paragraph (1) of the Article preserve any rights of the beneficiary under the undertaking”.

We have a comment on sub paragraph (b) of para. 1 of this article. Where there is agreement on the termination of the undertaking it is not necessary to make such

termination in the form stipulated in the undertaking nor in the form referred to in Article 7/2. Termination may be in any form agreed upon so long as such termination do not cause harm to the applicant or the instructing party.

As we have noted before, such means of termination or amendment do not usually occur between the guarantor/issuer and the beneficiary but rather between them and the principal/applicant who is always the link between them.

ICC uniform rules of demand guarantees contain similar provisions (Articles 23 and 24).

19. Article 12 relating to expiry stipulates that:

"The validity period of the undertaking expires:

"(a) At the expiry date, which may be a specified calender date or the last day of a fixed period of time stipulated in the undertaking, provided that, if the expiry date is not a business day at the place of business of the guarantor/issuer at which the undertaking is issued, or of another person or at another place stipulated in the undertaking for presentation of the demand for payment, expiry occurs on the first business day which follows;

"(b) If expiry depends according to the undertaking on the occurrence of an act or event not within the guarantor/issuer's sphere of operations, when the guarantor/issuer is advised that the act or event has occurred by presentation of the document specified for that purpose in the undertaking or, if no such document is specified, of a certification by the beneficiary of the occurrence of the act or event;

"(c) If the undertaking does not state an expiry date, or if the act or event on which expiry is stated to depend has not yet been established by presentation of the required document and an expiry date has not been stated in addition, when six years have elapsed from the date of issuance of the undertaking".

This provision is costly, because during the period of six years of limitation the guarantor will continue to charge the principal commissions upon the independent guarantee, a matter which is too costly. ICC uniform rules for demand guarantees is more accurate as such period do not exceed six months from certain dates defined in Article 4.

20. Article 13 relating to the determination of rights and obligations provides that:

"1. The rights and obligations of the guarantor/issuer and the beneficiary arising from the undertaking are determined by the terms and conditions set forth in the undertaking, including any rules, general conditions or usages specifically referred to therein, and by the provisions of this Convention.

"2. In interpreting terms and conditions of the undertaking and in settling questions that are not addressed by the terms and conditions of the undertaking or by the provisions of this Convention, regard shall be had to generally accepted international rules and usages of independent guarantees or stand by letters of credit practice".

Through this Article practice may combine to the Convention, the publications nos. 458 and 500 of the ICC as means of interpretation, being 'generally accepted

international rules and usages of independent guarantees or stand by letters of credit practice' even where such rules are not subject to specific reference in the undertaking or in the transaction as a whole. The US District Court for the Southern District of New York in a recent opinion (Koola v. Citibank N.A.) acknowledged the UCP as "an internationally accepted codification of banking practice and custom". (See Documentary Credit Insight Vol.1 No. 3 Summer 1995, p. 6).

21. Article 14 relating to the standard of conduct and liability stipulates that:

"1. In discharging its obligations under the undertaking and this Convention, the guarantor/issuer shall act in good faith and exercise reasonable care having due regard to generally accepted standards of international practice of independent guarantees or stand-by letters of credit.

"2. A guarantor/issuer may not be exempted from liability for its failure to act in good faith or for any grossly negligent conduct".

Such provisions are also found in the ICC uniform rules for demand guarantees in Article 15.

22. Article 15 relating to the demand provides that:

"1. Any demand for payment under the undertaking shall be made in a form referred to in paragraph 2 of Article 7 and in conformity with the terms and conditions of the undertaking.

"2. Unless otherwise stipulated in the undertaking, the demand and any certification or other document required by the undertaking shall be presented, within the time that a demand for payment may be made, to the

guarantor/issuer at the place where the undertaking was issued.

"3. The beneficiary, when demanding payment, is deemed to certify that the demand is not in bad faith and that none of the elements referred to in subparagraphs (a), (b) and (c) of paragraph (1) of Articled 19 are present".

Acting in good faith is presumed to be attested in the demand for payment at the time of presenting it. If the beneficiary has a bad faith, he will be liable to refund the payment he already received. The beneficiary is also deemed to certify that none of the cases of Article 19/1 are present; they relate to falsified documents, the undertaking is not due or the demand has no conceivable basis. This also means that if such certification was proved to be faulty, refund of the payment received can be subject of a claim directed to the beneficiary.

23. Article 16 relating to the examination of the demand and the documents provides that:

"1. The guarantor/issuer shall examine the demand and any accompanying documents in accordance with the standard of conduct referred to in paragraph 1 of Article 14. In determining whether documents are in facial conformity with the terms and conditions of the undertaking, and are consistent with one another, the guarantor/issuer shall have due regard to the applicable international standard of independent guarantee or stand by letter of credit practice.

"2. Unless otherwise stipulated in the undertaking or elsewhere agreed by the guarantor/issuer and the beneficiary, the guarantor/issuer shall have reasonable

time, but not more than seven business days following the day of receipt of the demand and any accompanying documents, in which to:

"(a) Examine the demand and any accompanying documents;

"(b) Decide whether or not to pay;

"(c) If the decision is not pay, issue notice thereof to the beneficiary.

"The notice referred to in subparagraph (c) above shall, unless otherwise stipulated in the undertaking or elsewhere agreed by the guarantor/issuer and the beneficiary, be made by teletransmission or, if that is not possible, by other expeditious means and indicate the reason for the decision not to pay".

This Article stipulates the application of the 'international standard of independent guarantee or stand by letters of credit practice'. It must be noted that Article 13 of the UCP 500 used the same expression and queries are still raised to have a definition of what is meant by it. ICC uniform rules for demand guarantees did not contain the provision of seven days for examination of documents feeling that in guarantees the matter must be quicker as examination does not need the same time as documentary credits.

24. Article 17 relating to payment stipulates that:

"1. Subject to Article 19, the guarantor/issuer shall pay against a demand made in accordance with the provisions of Article 15. Following a determination that a demand for payment so conforms, payment shall be made promptly, unless the undertaking stipulates payment on a

deferred basis, in which case payment shall be made at the stipulated time.

"2. Any payment against a demand that is not in accordance with the provisions of Article 15 does not prejudice the rights of the principal/applicant".

25. Article 18 relating to set off provides that:

"Unless otherwise stipulated in the undertaking or elsewhere agreed by the guarantor/issuer and the beneficiary, the guarantor/issuer may discharge the payment obligation under the undertaking by availing itself of a right of set off, except with any claim assigned to it by the principal/applicant or the instructing party".

26. Article 19 relating to exception to payment obligation stipulates that:

"1. If it is manifest and clear that:

"(a) Any document is not genuine or has been falsified;

"(b) No payment is due on the basis asserted in the demand and the supporting documents; or

"(c) Judging by the type and purpose of the undertaking, the demand has no conceivable basis, the guarantor/issuer, acting in good faith, has a right, as against the beneficiary, to withhold payment.

"2. For the purposes of subparagraph (c) of paragraph 1 of this Article, the following are types of situations in which a demand has no conceivable basis:

"(a) The contingency or risk against which the undertaking was designed to secure the beneficiary has undoubtedly not materialised;

"(b) The underlying obligation of the principal/applicant has been declared invalid by a court or arbitral tribunal, unless the undertaking indicates that such contingency falls within the risk to be covered by the undertaking;

"(c) The underlying obligation has undoubtedly been fulfilled to the satisfaction of the beneficiary;

"(d) Filfilment of the underlying obligation has clearly been prevented by wilful misconduct of the beneficiary;

"(e) In the case of a demand under a counter guarantee, the beneficiary of the counter guarantee has made payment in bad faith as guarantor/issuer of the undertaking to which the counter guarantee relates.

"3. In the circumstances set out in subparagraphs (a), (b) and (c) of paragraph 1 of this Article, the principal/applicant is entitled to provisional court measures in accordance with Article 20".

This Article will be always controversial. It revealed that the independent guarantee in the Convention is not equivalent to a first demand guarantee, as the issuer or guarantor has the opportunity to judge the demand of payment and to say that the beneficiary has no right to receive payment, and this threatens the independability of the guarantee. Also, the drafting of this Article leads to saying that bringing a lawsuit by the issuer against the beneficiary to denounce his right is a sufficient cause to stop payment of the undertaking. The matter is different with the ICC uniform rules for demand guarantees as the guarantor has nothing to do with the real reasons behind the demand for payment so long as the required documents are presented and the attestation required by Article 20 is submitted to the effect that the principal is in

breach and the respect in which he is in breach. Cases of fraud are the sole justifying non payment.

27. Article 20 relating to provisional court measures provides that:

"1. Where, on an application by the principal/applicant or the instructing party, it is shown that there is a high probability that, with regard to a demand made, or expected to be made, by the beneficiary, one of the circumstances referred to in subparagraphs (a), (b) and (c) of paragraph 1 of Article 19 is present, the court, on the basis of immediately available strong evidence, may:

"(a) Issue a provisional order to the effect that the beneficiary does not receive payment, including an order that the guarantor/issuer hold the amount of the undertaking; or

"(b) Issue a provisional order to the effect that the proceeds of the undertaking paid to the beneficiary are blocked, taking into account whether in the absence of such an order the principal/applicant would be likely to suffer serious harm.

"2. The court, when issuing a provisional order referred to in paragraph 1 of this Article, may require the person applying therefor to furnish such form of security as the court deems appropriate.

"3. The court may not issue a provisional order of the kind referred to in paragraph 1 of this Article based on any objection to payment other than those referred to in subparagraphs (a), (b) and (c) of paragraph 1 of Article 19, or use of the undertaking for a criminal purpose".

28. Article 21 relating to the choice of the applicable law stipulates that:

"The undertaking is governed by the law the choice of which is:

"(a) Stipulated in the undertaking or demonstrated by the terms and conditions of the undertaking; or

"(b) Agreed elsewhere by the guarantor/issuer and the beneficiary".

29. Article 22 relating to determination of the applicable law provides that:

"Failing a choice of law in accordance with Article 21, the undertaking is governed by the law of the State where the guarantor/issuer has that place of business at which the undertaking was issued".

30. Chapter seven contained final clauses in Articles 23 through 29 as follows:

Article 23 (Depositary): "The Secretary General of the United Nations is the depositary of this Convention". As to the ICC uniform rules for demand guarantees there is no depositary but the rules takes its force from reference made to them in demand guarantees together with the number of publication.

Article 24 (Signature, ratification, acceptance, approval, accession):

"1. This Convention is open for signature by all States at the Headquarters of the United Nations, New York, until....(the date two years from the date of adoption).

"2. This Convention is subject to ratification, acceptance or approval by the signatory States.

"3. This Convention is open to accession by all States which are not signatory States as from the date it is open for signature.

"4. Instruments of ratification, acceptance, approval and accession are to be deposited with the Secretary General of the United Nations".

Article 25 (Application to territorial units):

"1. If a State has two or more territorial units in which different systems of law are applicable in relation to the matters dealt with in this Convention, it may, at the time of signature, ratification, acceptance, approval or accession, declare that this Convention is to extend to all its territorial units or only one or more of them, and may at any time substitute another declaration for its earlier declaration.

"2. These declarations are to state expressly the territorial units to which the Convention extends.

"3. If, by virtue of a declaration under this article, this Convention does not extend to all territorial units of a State and the place of business of the guarantor/issuer or of the beneficiary is located in a territorial unit to which the Convention does not extend, this place of business is considered not to be in a Contracting State.

"4. If a State makes no declaration under paragraph 1 of this Article, the Convention is to extend to all territorial units of that State".

Article 26 (Effect of Declaration):

"1. Declarations made under Article 25 at the time of signature are subject to confirmation upon ratification, acceptance or approval.

"2. Declarations and confirmations of declarations are to be in writing and to be formally notified to the depositary.

"3. A declaration takes effect simultaneously with the entry into force of this Convention in respect of the State concerned. However, a declaration of which the depositary receives formal notification after such entry into force takes effect on the first day of the month following the expiration of six months after the date of its receipt by the depositary.

"4. Any State which makes a declaration under Article 25 may withdraw it at any time by a formal notification in writing addressed to the depositary. Such withdrawal takes effect on the first day of the month following the expiration of six months after the date of the receipt of the notification of the depositary".

Article 27 (Reservations):

"No reservations may be made to this Convention".

Article 28 (Entry into force):

"1. This Convention enters into force on the first day of the month following the expiration of one year from the date of the deposit of the fifth instrument of ratification, acceptance, approval or accession.

"2. For each State which becomes a Contracting State to this Convention after the date of the deposit of the fifth instrument of ratification, acceptance, approval or accession, this Convention enters into force on the first

day of the month following the expiration of one year after the date of the deposit of the appropriate instrument on behalf of that State.

"3. This Convention applies only to undertaking issued on or after the date when the Convention enters into force in respect of the Contracting State referred to in subparagraph (b) of paragraph 1 of Article 1".

Article 29 (Denunciation):

"1. A Contracting State may denounce this Convention at any time by means of a notification in writing addressed to the depositary.

"2. The denunciation takes effect on the first day of the month following the expiration of one year after the notification is received by the depositary. Where a longer period is specified in the notification, the denunciation takes effect upon the expiration of such longer period after the notification is received by the depositary".

Best regards.

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