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Dr. Boris Kozolchyk

**The Road to Nowhere: *Caterpillar v. Usinor* and CISG Claims by Downstream Buyers Against Remote Sellers**

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## Supply Chain Financing, Straight Bills of Lading and Standby Letters of Credit

Dr. Boris Kozolchyk\*

### I. Straight Bills of Lading and What the *Carewins* Decision Corrected

The 2009 decision by the Hong Kong Court of Final Appeal in *Carewins Development (China) Ltd. v. Bright Fortune Shipping Ltd & Anor* (hereafter *Carewins*) relied on Hong Kong, British and Commonwealth court decisions to address two important issues concerning the legal status of straight bills of lading.<sup>1</sup> The first was whether a straight bill of lading is a document of title. If it is, as the Hong Kong Court of Final Appeal held in *Carewins*,<sup>2</sup> the ocean carrier that issued it has the duty described in *The Rafaela*, a unanimous 2005 decision by the House of Lords, “not to release the goods without production of the bill of lading, such duty arising as an incident of the instrument itself.”<sup>3</sup>

The second issue pertains to a clause in the bill of lading that disclaimed the carrier’s liability for misdelivery of the goods. The Court of Final Appeal of Hong Kong construed this clause against its drafter (*contra proferentum*) and found it insufficiently explicit to exempt the carrier from liability for its breach of the duty to require the presentation of the straight bill.<sup>4</sup>

These aspects required correction because two widely-quoted and relied-upon treatises in Great Britain and the British Commonwealth, *Benjamin's Sale of Goods* and *Carver on Bills of Lading*, contained Professor Guenter Treitel’s assertion that a straight bill “was not a symbol of the goods because the carrier was entitled and bound to deliver the goods to the named consignee without production of the bill.”<sup>5</sup>

Professor Treitel’s assertion, however, does not reflect international maritime practices. In preparation for a first draft of the transport document

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<sup>1</sup> [2009] 5 H.K.C. 160 (H.K.F.A.R.).

<sup>2</sup> *Id.* at 161, ¶2.

<sup>3</sup> *Id.* at 162, ¶7 (citing *J.I. Macwilliam Co. v. Mediterranean Shipping Co. SA (The Rafaela S)*, [2005] UKHL 11, 2 A.C. 423 (appeal taken from Eng.)).

<sup>4</sup> *Id.*

<sup>5</sup> *Id.* at 187.

provisions of UCP 500, the author interviewed French, German, Scandinavian, Latin American and United States carriers and freight forwarders and all regarded order, as well as straight, bills of lading as documents of title. They also called attention to the increased usage of sea waybills, especially in Scandinavian and inter-European shipments. As with rail, truck and air waybills and unlike straight bills of lading, sea waybills evidence receipt of the goods for carriage but are not documents of title. Accordingly, they do not have to be presented in order to obtain the delivery of the goods; mere identification of the consignee suffices to obtain delivery.

Eventually, courts familiar with these international practices, especially in Asian trade centers, abandoned the receipt characterization of the straight bill of lading. For example, a 2002 decision by the Singapore Court of Appeal<sup>6</sup> acknowledged Professor Treitel's views, but concluded that the delivery of a car to the named consignee of a straight bill of lading without requiring surrender of the bill of lading was unlawful and subjected the carrier who did not require the straight bill of lading to liability for damages. As pointed out by *Carewins*,<sup>7</sup> at the time the Singapore court was hearing the 2002 appeal, the lower court in *The Rafaela* had just decided against the carrier-issuer of a straight bill who delivered the cargo without requiring its surrender. The above-quoted language by the House of Lords in *The Rafaela* was, no doubt, a definitive step in the alignment of English case law with international straight bill of lading practice.

*Carewins* and *The Rafaela* may well provide the basis for the harmonization of English and Commonwealth law with international bill of lading law on the legal nature and status of straight bills as documents of title. A related and important aspect concerns the harmonization of laws and practices on the security interests of the consignor, consignee and secured creditors who rely on straight bills of lading as collateral for their respective advances or loans. This is particularly true with respect to the consignor and consignee's transfer, assignment or pledge of their respective rights in the straight bill of lading and goods covered by it to a secured lender.

This paper argues that the harmonization of international bills of lading law on the status of straight bills as documents of title and the adoption of U.C.C. Article 9 concepts by an increasing number of Latin American, European and Asian jurisdictions now allow straight bills of lading, in electronic or paper-based form, to function as reliable collateral in

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<sup>6</sup> APL Co. v. Voss Peer, [2002] 4 S.L.R. 481, 2 Lloyd's Rep 707 (C.A.) (Sing.).

<sup>7</sup> *Carewins*, *supra* note 1, at 188, ¶90.

letters of credit and non-letter of credit transactions. Serving as documents of title, straight bills of lading can provide a safe means by which banks can finance the international shipping of goods and secure payment and reimbursement of commercial or standby letter of credit payments, especially in the context of what will be described in this article as “supply chain financing.”

Part I of the paper briefly examines the relevant United States law and practice on the use of straight bills as collateral prior and subsequent to the enactment of Article 9 of the Uniform Commercial Code (U.C.C). The reason for focusing on United States secured transactions law and practice is that it has had vast experience with bills of lading as collateral and presently serves as a model for harmonization of this law. Yet, after examining the rights and defenses to claims based on freight forwarders’ (or “contractual” carriers’) straight bills of lading, Part II shows that these documents are not reliable collateral. As illustrated by *Carewins*, the carrier can prevent *in personam* actions by the holders of freight forwarders’ straight bills of lading. In addition, Part III shows that *in rem* actions by the holders of freight forwarders’ straight bills of lading are also an uncertain means with which to seek the attachment of the goods or their carrying vessel. In contrast, bills of lading issued by ship owners or fully-fledged (“actual” as contrasted with “contractual”) carriers are effective tools with which to obtain those attachments.

Finally, Part IV addresses the future of straight bills of lading as reliable collateral. It argues that the law of letters of credit contained in Revised UCC Article 5 and of secured financing in Article 9 of the same code provides an additional safety element to further ensure that straight bills of lading serve as reliable collateral, especially for supply chain financing.

## **II. The Development of United States Law and Practice Concerning Straight Bills of Lading as Collateral**

The dichotomy of negotiable and straight bills of lading appeared first in the Federal Bill of Lading (Pomerene Act) of 1916.<sup>8</sup> This statute

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<sup>8</sup> The Federal Bill of Lading (Pomerene) Act of 1916, ch. 415, Pub. L. No. 239, 39 Stat. 538 (1916) (currently codified in 49 U.S.C. §§ 80101 – 80116). This statute governs bills of lading issued by any common carrier for the transportation of goods in any territory of the United States, or the District of Columbia, or from a place in a State to a place in a foreign country, or from a place in a State to a place in another State, or from a place in the same State through another State or foreign country. 39 Stat. at 538–39, §1.



governs generically all of the bills of lading used in interstate commerce in the United States.<sup>9</sup> As noted by a state appellate court, the primary purpose of this statute was:

[T]o confer complete negotiability on certain types of bills (order bills) and to change the rule referred to, in so far as it applied to order bills. Negotiability was not conferred on order bills in express terms but the implication of negotiability is obvious when the entire act is considered.<sup>10</sup>

This particular feature distinguished United States negotiable bills of lading from their English, Commonwealth and civil law counterparts and did this until many of these countries adopted a version of the Hague Convention that contained the same rule.<sup>11</sup> The Pomerene Act version of negotiability thus sanctioned a negotiable bill of lading that was not only a document of title, but also a fully “abstract” or “independent” undertaking. Possession of such a bill of lading in the hands of a *bona fide* purchaser or lender such as the bank that issued or negotiated a letter of credit and its documents assured them of the carrier’s liability to deliver the goods shipped or their market value, even if the consignor had not actually shipped the goods described in the bill of lading. For what mattered as the carrier’s abstract obligation was the description of the goods in the bill of lading and not the equities of underlying transactions. It is for this reason that the author noted in another publication that with the early 20<sup>th</sup> century enactment of the Uniform Bills of Lading and Pomerene Acts, bills of lading subject to United States law were the most desirable anywhere in the trading and finance world.<sup>12</sup> Together with the scarcity of manufactured products and of carrying vessels in Europe following World War I, the quality of United States issued ocean bills of lading made it possible for United States banks and ocean carriers to become the most prominent participants in

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<sup>9</sup> *Id.*

<sup>10</sup> *Chesapeake & O. R. Co. v. State Nat'l Bank of Mayville*, 138 S.W.2d 511, 513 (Ky. 1939).

<sup>11</sup> Boris Kozolchyk, *Evolution and Present State of the Ocean Bill of Lading from a Banking Law Perspective*, 23 J. OF MAR. L. & COM. 161, 173–77, 185–90 (1992).

<sup>12</sup> *See id.* at 173–75 (“With the early 20th century enactment of the Uniform Bill of Ladings and Pomerene Acts in the United States, American-issued bills of lading attained the highest level of abstraction available at that time . . . [the right to claim the value of the described goods] instilled trust in the written statements by carriers and encouraged consignees to deal with distant and unknown sellers.”).

international trade and particularly in the issuance, confirmation and negotiation of letters of credit.<sup>13</sup>

In addition to bolstering the negotiability of “order” or “bearer” bills of lading, the Pomerene Act was the first to confer a restricted negotiability status to straight bills of lading. In § 2, it defined a straight bill as: “A bill in which it is stated that the goods are consigned or destined to a specified person . . . .”<sup>14</sup> This bill was deemed a document of title that lacked the necessary “order” or “bearer” clause to be fully negotiable, but which nonetheless could be transferred or negotiated in a restricted sense. Indeed, § 109 of the Pomerene Act provided for its transfer by delivery and for a restricted version of negotiation. Under the heading “Transfer of Bill by Delivery; negotiation of straight bill”, this section provided that:

A bill may be transferred by the holder by delivery, accompanied by an agreement, express or implied, to transfer title to the bill or to the goods represented thereby. A straight bill of lading cannot be negotiated free from existing equities, and the endorsement of such a bill gives the transferee no additional right.

§ 112 in turn added that a person to whom a bill has been transferred, but not negotiated, acquired — as against the transferor — title to the goods, but subject to the terms of any previous agreement with the transferor. Thus, if the bill was a straight bill, the transferee acquired the right to notify the carrier of the transfer and become “the direct obligee of whatever obligations the carrier owed to the transferor of the bill *immediately before the notification.*”<sup>15</sup> This meant that the transferees’ claim to such a carrier obligation could be defeated by “garnishment or by attachment or execution upon the goods by a creditor of the transferor, or by a notification to the carrier by the transferor or a subsequent purchaser from the transferor of a subsequent sale of the goods by the transferor.”<sup>16</sup> The fact that the enforcement of these rights *in rem* depended upon the time creditors claimed their liens and notified the carrier of the creation of their security interest closely resembled the role of the creditor-assignee’s notification to the account-debtor of his status as an assignee in the law of assignment of

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<sup>13</sup> See Wilbert Ward, *AMERICAN COMMERCIAL CREDITS*, at 7 (1922, The Ronald Press, Nabu Public Domain Reprints. The author is indebted to Professor James E. Byrne for having made this copy available).

<sup>14</sup> The Federal Bill of Lading (Pomerene) Act of 1916, 39 Stat. at 539, §2.

<sup>15</sup> 39 Stat. at 543, §32, ¶ 1 (emphasis added).

<sup>16</sup> *Id.* §32, ¶ 2.

contract rights.<sup>17</sup> Not surprisingly, some United States courts equated the status of the transferee of a straight bill to that of an assignee of the transferor's contractual rights against the carrier.<sup>18</sup>

The empowerment of the straight bill of lading as a document of title capable of being transferred or assigned, albeit subject to underlying equities and notification, was soon reflected in practices designed to utilize the possessory rights of the holders of these bills as collateral for loans extended mostly by banks and factoring enterprises. For example, in one such a practice, the shipper was both the consignor and consignee of the cargo who according to a federal court decision retained "ownership and control of the shipment until it reached its destination, and even there before delivery had been made and possession parted with."<sup>19</sup> In that case, the shipper in Iowa no longer trusted his broker-factor in Philadelphia to pay for the cargo of poultry before reselling it. The shipper would have preferred an order bill of lading issued to his own order, but the rail carrier said that he could not issue such a negotiable bill for a cargo of chicken.<sup>20</sup> The shipper then accepted a straight bill of lading in which he as consignor was also the consignee.<sup>21</sup> This scheme enabled him to retain possession of the cargo at destination until the unnamed consignee would pay for it.<sup>22</sup>

As in *Carewins* and *The Rafaela* (although some 70 years earlier), the Circuit Court of Appeals for the Eighth Circuit held the carrier liable for allowing the broker-factor (as a notify party) to obtain possession of the cargo without surrendering the straight bill.<sup>23</sup> However, from a secured transactions law and practice standpoint what mattered most in this case

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<sup>17</sup> See JAMES E. BYRNE, NEGOTIABILITY, THE DOCTRINE AND ITS APPLICATION IN US COMMERCIAL LAW 1-11 (14th ed. 2005) (providing an illuminating discussion of the differences between the law of transfers and assignments and that of negotiation in the United States; and especially addressing the insight provided by the decision in *American Bridge Co. of New York v. City of Boston*, 88 N.E. 1089 (Mass. 1909) into why contract law is inadequate to address certain "transfer" issues from buyers of promises that want streamlined or supercharged rights).

<sup>18</sup> See, e.g., *Quality Shingle Co. v. Old Or. Lumber & Shingle Co.*, 187 P. 705, 706 (Wash. 1920) ("[T]he language of [The Federal Bill of Lading (Pomerene) Act of 1916] plainly places the assignee of a straight bill of lading in all respects in the shoes of his assignor.").

<sup>19</sup> See *Estherville Produce Co. v. Chicago R.I. & P.R. Co.*, 57 F.2d 50, 52 (8th Cir. 1932).

<sup>20</sup> *Id.* at 51.

<sup>21</sup> *Id.*

<sup>22</sup> *Id.* at 52 ("It is to be kept in mind that, in this straight bill of lading the produce company was named both as consignor and consignee, thus, in any view, retaining ownership and control of the shipment until it reached its destination, and even there before delivery had been made and possession parted with.").

<sup>23</sup> *Id.* at 52-53.

was the principle that an ownership or security interest in the same collateral represented by a straight bill of lading could be retained by the consignor and could also be transferred to another or could be held by the same consignor whether as an owner of the goods or as a secured creditor.

The significance of the consignor's ability to transfer or assign his rights in the bill of lading to another party, including to oneself as a consignee-creditor or to an arm's length secured creditor for enabling straight bills of lading to serve as reliable collateral became apparent in *George F. Hinrichs* (hereafter *Hinrichs*) v. *Standard Trust & Savings Bank*, (hereafter *Standard Bank*), a decision rendered by the Circuit Court of Appeals for the Second Circuit in 1922, only six years after the enactment of the Pomerene Act.<sup>24</sup> In that decision, Grant, a Chicago wholesaler of butter, eggs and poultry, shipped a carload of eggs by rail consigned to *Hinrichs*. Grant obtained from *Standard Bank* a sight draft payable to its order and drawn against *Hinrichs*. This draft was accompanied by the straight bill of lading procured by Grant that covered the shipment of eggs consigned to *Hinrichs*. *Standard Bank*, acting as a lender to Grant, credited his account with the amount of the draft drawn against *Hinrichs* and forwarded the bill of lading accompanied by a sight draft and an invoice for the amount he owed to *Standard Bank's* correspondent bank in New York.<sup>25</sup> The latter's function was to present these documents to *Hinrichs* and demand his payment against the release of the straight bill of lading. During the late nineteenth and early twentieth centuries, the presentation of a sight draft accompanied by the straight bill of lading had become the standard procedure for "documentary collection" transactions in the United States, Europe and other major trading centers until eventually it was largely replaced by the commercial letter of credit.<sup>26</sup>

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<sup>24</sup> 279 F. 382, 384–86 (2d Cir. 1922).

<sup>25</sup> *Id.* at 383–84.

<sup>26</sup> *See id.* at 388–89.

In Williston on Sales, Sec. 289, that writer, discussing the practice of a shipper's attaching the draft to a bill of lading, whether he has the draft discounted or not, and their being then sent forward and presented to the party to whom the merchandise is forwarded, says: 'So common has this practice become that the mere fact that a bill of lading and a draft are attached together indicates that the shipper intends to make the delivery of the goods conditional upon the payment of the draft. This rule is accordingly enacted in the Sales of Goods Act and the English provision is copied in the American Sales Act (subdivision 4 of section 20). The authorities collected in the note show that the courts have fully recognized the meaning and validity of the mercantile custom.'

In this case, *Hinrich* as consignee refused to pay for the eggs but nonetheless somehow (in a manner not explained by the court) received the goods from the carrier and sold them to a third party, collected their price, deducted from it an amount it claimed that Grant owed him and forwarded the remainder to Grant. When sued by *Standard Bank* for the value of the shipment represented in the straight bill of lading, he claimed that he should not have had to pay twice for the same eggs.<sup>27</sup>

The Circuit Court of Appeals for the Second Circuit referred to the above-transcribed sections of the Pomerene Act to set forth two principles that define the rights of a holder of a straight bill in the cargo: First, the straight bill may be transferred by its holder by delivery, accompanied by an agreement “express or implied to transfer the title to the bill or to the goods represented thereby” but subject to existing equities.<sup>28</sup> And second, the transferee acquires thereby, “as against the transferor the title to the goods, subject to the terms of any agreement with the transferor (and in the case of straight bill, the transferee) . . . the right to notify the carrier of the transfer to him of such bill and thereby become the direct obligee of whatever obligations the carrier owed to the transferor of the bill immediately before the notification.”<sup>29</sup>

The court pointed out that *Standard Bank* as transferee or assignee of the straight bill of lading had not notified the carrier as the Pomerene Act required.<sup>30</sup> Under these circumstances, the question was whether *Hinrichs* as Grant’s consignee-factor of the shipment was legally entitled to sell the cargo after he had another type of notice that the bill of lading had been transferred to *Standard Bank*. The court relied on “mercantile law” as the source for the following rule:

Where A, the shipper, takes a bill of lading and names himself as consignee, he retains title to the goods. If he names B as consignee, the title to the goods is in B. But in both cases he has an effective hold upon the goods, for in the latter case he has a right of possession analogous to a lien, which he can exercise prior to the delivery of the goods to B by the carrier.<sup>31</sup>

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<sup>27</sup> *Id.* at 384.

<sup>28</sup> *Id.* at 385–86.

<sup>29</sup> *Id.* at 385 (parenthesis added).

<sup>30</sup> *Id.*

<sup>31</sup> *Id.* at 386.

The court acknowledged that “the vital question is as to the right of Standard Trusts & Savings Bank, which acquired the straight bill of lading from the shippers by having discounted it.”<sup>32</sup> It also acknowledged that the bank took the rights of the shippers subject to equities and therefore did not acquire the legal title to the eggs. That title as indicated by the bill belonged to the consignee *Hinrichs*. However, evidence also showed that the consignee was in fact holder of a merely naked title, the eggs having been consigned to him to sell for the consignor, who remained the beneficial or equitable title holder.

The court concluded that if the consignee *Hinrichs*, after having notice that the consignor had parted with its interest and transferred its rights to the bank, sold the eggs and paid the proceeds over to the consignor, it was liable to the bank which had succeeded in whatever rights the consignor possessed and of which it received notice. The right of the bank as a secured creditor, then was not impaired by whatever took place after this notice between the consignor and the consignee.<sup>33</sup>

After reviewing the large number of cases involving the above-described practices, the court quoted Williston on Sales for the proposition that the discount of the documentary drafts had become so common that the mere fact that a bill of lading and a draft are attached together evidenced that the shipper intended to make the delivery of the goods conditional upon payment of the draft. Accordingly, when *Hinrichs* ignored such a notice he acted at his peril.<sup>34</sup> *Certiorari* was denied by the United States Supreme Court and the Shepard’s citator indicates that this case remained the law of the land having been cited without reservation in almost a dozen federal and state decisions until the advent of the U.C.C. in 1952 and its progressive enactment by all of the fifty states.<sup>35</sup>

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<sup>32</sup> *Id.*

<sup>33</sup> *Id.* at 389–90.

<sup>34</sup> *Id.*

<sup>35</sup> *Hinrichs*, 279 F. 382, *cert. denied* 258 U.S. 629 (1922). The following federal and state cases cited *Hinrichs* for support. *Austin Nichols & Co. v. S.S. Isla De Panay*, 292 F. 723, 731 (2d Cir. 1923); *Yakima Trust Co. v. Taub (In re Taub)*, 4 F.2d 993, 995 (2d Cir. 1924); *Sugarland Indus. v. Old Colony Trust Co.*, 6 F.2d 203, 207 (5th Cir. 1925); *Estherville Produce Co. v. Chicago R. I. & P. R. Co.*, 57 F.2d 50, 52 (8th Cir. 1932); *G. A. C. Commercial Corp. v. Wilson*, 271 F. Supp. 242, 246 (S.D.N.Y. 1967); *Kasden v. The New York, New Haven, & Hartford R.R. Co.*, 133 A. 573, 575 (Conn. 1926); *Chesapeake & Or. Co. v. State Nat'l Bank of Maysville*, 133 S.W.2d 511, 515 (Ky. 1939); *Pa. R.R. Co. v. Edson Bros.*, 92 Pa. Super. 496, 498 (1927); *E. Tex. Motor Freight Lines v. W. H. Hutchinson & Son, Inc.*, 241 S.W.2d 759, 765 (Tex. Civ. App. 1949); *Mumford v. Hartford Accident & Indem. Co.*, 228 P. 206, 210 (Utah 1924).

Revised Articles 1, 7 and 9 of the U.C.C. made reliance on bills of lading as collateral easier and more certain. Article 1 defined bills of lading generically as documents of title.<sup>36</sup> In turn, Article 7 defines the term “document” as a “document of title” or as a transportation receipt document of the type described in Section 7-201(b) (Person That May Issue a Warehouse Receipt; Storage Under Bond)<sup>37</sup> and listed both negotiable and non-negotiable bills of lading as documents of title.<sup>38</sup> Revised Article 9 defined collateral as “the property subject to a security interest or agricultural lien” including, among other, “accounts, chattel paper, payment intangibles, and promissory notes . . . .”<sup>39</sup> An Article 9 chattel paper is one that enables a secured creditor to rely both on the *in personam* liability of a negotiable instrument such as a promissory note and the accompanying and often attached *in rem* liability in the goods.

From its inception, Article 9 formulated what by now has become an important principle of the law of secured transactions: title to the collateral is immaterial.<sup>40</sup> By doing this, the U.C.C. eliminated the need for ambiguous and often counter-intuitive distinctions between legal and equitable title and who holds which; is it the “historical” owner of the goods, the secured creditor or the secured debtor, or all of these parties? This was a distinction relied on by the *Hinrich* court among others.<sup>41</sup> Finally, Article 9 provided a filing alternative to the notice to the carrier required from the secured creditor who relied on a bill of lading as collateral. As a result of this alternative, notice to third parties (creditors as well as *bona fide* purchasers) is available by a filing in an easily accessible, inexpensive and specially-designed registry for notices of security interests in personal property.<sup>42</sup>

Where the security interest was in a negotiable document and it concerned goods in the possession of the carrier-bailee who issued the negotiable documents covering the goods, the security interest in the goods could be perfected by perfecting a security interest in the negotiable document as just described. This security interest has priority over any security interest in the goods that becomes perfected by “any other methods

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<sup>36</sup> See U.C.C. § 1-201(6) (General Definitions) (2010).

<sup>37</sup> See *id.* § 9-102(a)(30) (Definitions and Index of Definitions).

<sup>38</sup> See *id.* § 7-104 (Negotiable and Nonnegotiable Document of Title).

<sup>39</sup> See *id.* § 9-102(a)(12) (Definitions and Index of Definitions).

<sup>40</sup> See *id.* § 9-202 (Title to Collateral Immaterial) (stating the present formulation of the principle).

<sup>41</sup> See *id.*

<sup>42</sup> See *id.* § 9-501 (Filing Office).

during that time.”<sup>43</sup> Where the security interest is in goods covered by a non-negotiable document such as a straight bill, and the goods are in the possession of the carrier who issued the non-negotiable document, the security interest in these goods is perfected by: (1) issuing a document in the name of the secured party, *i.e.*, the straight bill of lading; (2) the carrier-bailee’s receipt of the notification of the secured party’s interest or (and this is an important “or”); (3) by the secured creditor filing as to the goods.<sup>44</sup>

U.C.C. § 9-110 (Security Interests Arising Under Article 2 or 2A) also recognizes a security interest arising under U.C.C. § 2-505 (Seller’s Shipment Under Reservation) and protects the consignor until the consignee receives possession of the goods. U.C.C. Article 2 on Sales also strengthens the role of the non-negotiable bill of lading as collateral. § 2-505(1)(b) provides for the preferential right of the consignor to the goods shipped under a non-negotiable bill of lading as against the consignee and his creditors.<sup>45</sup> And § 2-505(1)(a) adds that a negotiable bill of lading issued to the name of the consignor reserves possession of the goods as security.<sup>46</sup>

### **III. Rights and Defenses to Claims Based on Freight Forwarders’ Straight Bills of Lading**

The reliability of straight bills of lading as collateral decreases significantly when issued by transportation intermediaries known as freight forwarders or “contractual” carriers. As intermediaries between the ship-owners and the shippers, freight forwarders may rent or purchase shipping space from the ship-owners through charter party agreements. In the United States and a few other countries, freight forwarders can also act as common carriers and, as such, publish tariffs, issue bills of lading in accordance with these tariffs and make themselves available for the transportation of goods of the public at large, rather than just for select clients. These freight

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<sup>43</sup> See *id.* § 9-312(c)(1); § 9-312(c)(2) [Goods covered by negotiable document.].

<sup>44</sup> See U.C.C. § 9-312(d) [Goods covered by nonnegotiable document.].

<sup>45</sup> *Id.* § 2-505(1)(b) (Seller’s Shipment Under Reservation) (“(1)Where the seller has identified goods to the contract by or before shipment: . . . (b) a non-negotiable bill of lading to himself or his nominee reserves possession of the goods as security . . .”).

<sup>46</sup> *Id.* § 2-505(1)(a) (Seller’s Shipment Under Reservation) (“(1) Where the seller has identified goods to the contract by or before shipment: (a) his procurement of a negotiable bill of lading to his own order or otherwise reserves in him a security interest in the goods.”).



forwarders are known as Non Vessel Owning or Operating Common Carriers (NVOCCs for short).<sup>47</sup>

All of the bills of lading issued by the freight forwarders have one aspect in common: the *in personam* and *in rem* rights they can confer upon their holders are “derivative”, *i.e.*, the rights of the holders of bills of lading issued by freight forwarders are derived from the charter party entered into between the owner or operator of the vessel (on behalf of the owner) and the freight forwarder as a charterer. More often than not, this derivation is indicated by expressions such as “per charter party” or “subject to charter party.” The derivative nature of these documents can deprive their holders of *in rem* rights against the vessel or the cargo or can subject these rights to major pre-existing liability of the freight forwarder charterer to the shipowner, such as for charges as major as those for “demurrage.”<sup>48</sup> It can also subject their holder, such as a bank that relied on them as collateral, to *in personam* defenses that can equally preclude its claim against the carrier.

#### **A. Defenses Against *In Personam* Actions**

As an example of a defense available to the carrier against an *in personam* action by the holders of freight forwarders’ straight bills of lading, consider the following facts in *Carewins*. The Court of Final Appeal found that the defendant, a freight forwarder and a “contractual” carrier (hereafter BF), issued two sets of bills of lading to the shipper-respondent *Carewins*. Both sets named *Carewins* as the shipper and its buyer as the consignee and also as the notify party (hereafter AFI). Once in Los Angeles, the containers were handled by freight forwarders (hereafter TUG) who acted as agents for BF in the discharge and delivery of the containers to AFI.

Shortly after this delivery, the goods were seized by US Marshalls executing a United States federal court order that resulted from infringement of trademark proceedings brought by Burberry Ltd, a fashion

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<sup>47</sup>See Don Hofstrand, Transportation Terms, Co-director, Ag Marketing Resource Center, Transportation Terms (Oct. 2006), [www.agmrc.org/business\\_development/getting\\_prepared/valueadded\\_agriculture/glossaries\\_of\\_terms/transportation\\_terms.cfm](http://www.agmrc.org/business_development/getting_prepared/valueadded_agriculture/glossaries_of_terms/transportation_terms.cfm); [www.somatrans.mu/glossary/N/](http://www.somatrans.mu/glossary/N/); [www.asmara.com/terminology.htm](http://www.asmara.com/terminology.htm) (describing the various services provided by NVOCCs).

<sup>48</sup>See, *e.g.*, *Mineral v. Commonwealth Oil Ref. Co. (In re Commonwealth Oil Ref. Co.)*, 734 F.2d 1079 (5th Cir. 1928) (illustrating the importance of demurrage charges and their allocation per charter party stipulations).

house, against AFI.<sup>49</sup> Burberry's action against AFI was later settled out of court and the goods disposed of on terms which were not revealed at the trial. The Court also deemed established the fact that AFI never paid *Carewins* for the goods it had shipped.<sup>50</sup>

The Court did not determine why the consignee did not pay the shipper, nor the terms of the settlement between Burberry and AFI and whether they also involved *Carewins* as an unnamed defendant. The fact that AFI paid nothing for the goods it obtained from the BF would support the allegation that *Carewins* and AFI were part of the same legal entity that conspired to infringe Burberry's trademark. If true, this allegation would explain *Carewins*' lack of interest in obtaining payment from the consignee for the goods delivered to him without the latter's tender of his straight bill of lading. It would also explain why *Carewins* seemed willing to delegate the task of demanding the presentation of the straight bill of lading in exchange for presumably the payment of cash on delivery, not to the customarily trusted intermediaries such as a collecting bank or a bank that issued a letter of credit on behalf of AFI, but to a freight forwarder.

If BF were to provide *prima facie* evidence of such a conspiracy and of its own innocence with respect to it, it would have a valid defense against a holder of the straight bill of lading issued to *Carewins* as well as against his transferees or assignees. The aforementioned set of facts shows that contractual equities or violations of the law that took place between the consignor and consignee of the freight forwarder's straight bill of lading would be available to the carrier as defenses in an *in personam* action.

## **B. Defenses Against *In Rem* Actions**

As is well known to international maritime traders and experienced bankers, an ocean bill of lading issued by a ship owner or shipping company-carrier is easier to enforce against the carrier, his ship and the cargo than the one issued by a freight forwarder. An old principle of the law of bills of lading of French origin suggests the explanation for this ease: "the vessel is bound to the merchandise and the merchandise is bound to the vessel" (*Le batel est obligé a la merchandise, et la merchandise au batel*).<sup>51</sup> The procedural meaning of this principle is that the consignee or other cargo claimant in possession of a negotiable or straight bill of lading issued

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<sup>49</sup> See *Carewins*, *supra* note 1, at 166, ¶ 12.

<sup>50</sup> *Id.* at 166, ¶ 13.

<sup>51</sup> GRANT GILMORE & CHARLES LUND BLACK JR., *THE LAW OF ADMIRALTY* 187 (2d ed. 1975) (citing the French commentator Cleirac).

by an owner or by the master of the vessel on behalf of its owner could seize, arrest, or attach the vessel to reimburse himself for damage or loss suffered by his cargo — for ownership of the vessel, whether “legal” or “beneficial,” provides the legal basis for an *in rem* action. In contrast, if the cargo claimant had a receipt type of document issued, say, by the ship’s mate or held a freight forwarder’s bill of lading issued by a charterer of the vessel, his rights against the vessel and the cargo would depend upon how much of a beneficial ownership interest such a contractual carrier would have when operating the vessel. This is not an easy determination and one that often varies from country to country.

Indeed, *in rem* actions do not tend to provide a reliable means of enforcing bills of lading. In 1990, during the drafting of UCP 500, the author surveyed maritime lawyers of various representative countries and jurisdictions on the enforceability of freight forwarders’ bills of lading to obtain the attachment of the cargo or the seizure of the vessel, and alternatively, whether the insurance policies they carried to pay for damages or losses suffered by the cargo were sufficient to cover these losses. The survey led to the conclusion that the right to claim possession of the goods from the carrier or to attach his vessel in an *in rem* action was regarded generally as belonging only to the freight forwarder who chartered or bought space in the vessel as the holder of the actual carrier’s bill of lading. Only rarely were these rights recognized as belonging to the holder of the bills issued by the freight forwarder. Thus, the derivative rights of the holder of the forwarder’s bill of lading were as uncertain in the surveyed countries and jurisdictions as was the adequacy of the freight forwarders’ insurance coverage.<sup>52</sup>

The author is not familiar with the amount of present insurance coverage among representative freight forwarders’ bills of lading, and it may well have increased since my 1990 survey.<sup>53</sup> Neither has the author been able to ascertain how much of the *in rem* liability law surveyed in the early nineteen nineties has changed in the intervening years. Yet, there are other contemporary indications that the derivative rights of the holders of

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<sup>52</sup> See Boris Kozolchyk, *The Unwarranted Comeback of the FIATA Bill of Lading*, DCInsight Vol. 11 No.2 Apr.-June 2005, at n.13, reprinted in 2006 ANNUAL SURVEY OF CREDIT LAW & PRACTICE 135–44 (James E. Byrne & Christopher S. Byrnes eds., 2006).

<sup>53</sup> In 1990, the average coverage of individual and associations of freight forwarders’ insurance policies did not exceed \$40,000 per average cargo. This was not a very reassuring coverage for cargo whose average price exceeded \$200,000. (This information was obtained through interviews with freight forwarders, shippers, and consignees during the years the author was at the ICC (the summer of 1990). The countries were France, Belgium, Sweden, and the United States.)

these bills remain uncertain and conflicting from one country or jurisdiction to another. For example, consider the differences in the law and practice concerning claims against vessels for damaged or lost cargo picked up in ports such as Hong Kong and Singapore. As described by Ian Koh, currently the head of the Shipping & International Trade Practice and a partner in the Litigation & Dispute Resolution Group at the Singapore law firm of WongPartnership, and formerly a shipping partner at Drew Napier, an active maritime law practitioner and litigator in that region:<sup>54</sup>

[T]he ownership of the offending vessel may change shortly after the (occurrence of the cargo) loss. If a writ in rem is not issued before the change of ownership and if there are no sister ships to the offending ship, then a claimant may find itself without a remedy in rem if he has no opportunity to arrest the vessel as security for his claim. In a one ship company situation, the consequences can be dire.<sup>55</sup>

Further, consider the situation of bills of lading issued as a result of a demise or bare boat charter parties. In Singapore, the general rule is that if the offending ship is under a demise charter where the charterer hires his own crew and operates the vessel with them at the time the damage occurred, then that ship is free from arrest for the cargo claim.<sup>56</sup> Yet, Ian Koh also points out that under English and Hong Kong law, arrest or seizure of such a chartered vessel may still be available.<sup>57</sup> In addition, key concepts such as beneficial ownership of the vessel as contrasted with its

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<sup>54</sup> See Ian Koh (ian.koh@wongpartnership.com), Former Shipping Partner at Drew Napier, Current Issues in Our Admiralty/Shipping Practice, at ¶ 5, [http://www.drewnapier.com/publications/D\\_npub-4.pdf](http://www.drewnapier.com/publications/D_npub-4.pdf) [hereinafter Current Issues in Our Admiralty/Shipping Practice].

<sup>55</sup> *Id.* (parenthesis added).

<sup>56</sup> *Id.* ¶ 19. Mr. Koh explains that determining whether the contractual carrier is a demise charterer is especially important under Singapore Law because of the peculiarities of Singapore's High Court (Admiralty Jurisdiction) Act which confers admiralty jurisdiction on the Singapore court. *Id.* ¶ 18 (quoting High Court (Admiralty Jurisdiction) Act, *infra* note 49, §4(4)(a)(b)(i)(ii)). Thus, if the contractual carrier is the beneficial owner of the vessel carrying the cargo at the time it was damaged, then the cargo claimant can arrest the offending ship to secure his claim. Alternatively, he can also arrest other ships beneficially owned by the contractual carrier. If the contractual carrier is a demise charterer of the offending ship, then the offending ship cannot be arrested for the cargo claim. Only the ships beneficially owned by the demise charterer can be arrested. *Id.* ¶ 19.

<sup>57</sup> *Id.* ¶ 6. A perhaps determinant consideration is who signed the bill of lading and for whom or on whose behalf, the owner of the vessel or the charterer. See *id.* ¶ 7 (citing *Wilston SS Co. v. Andrew Weir & Co.* (1925) 22 Lloyd's Rep. 521; *Cascade Shipping Inc. v. Eka Jaya Agencies (Pte) Ltd* [1993] 1 S.L.R. 980 (Sing.)).

legal ownership are only indirectly and vaguely defined. For example, Section 4(4) of Singapore's High Court (Admiralty Jurisdiction) Act governs the availability of *in rem* actions and forms of ownership as follows:

In the case of any such claim as is mentioned in section 3 (1) (d) to (q), where —

(a) the claim arises in connection with a ship; and

(b) the person who would be liable on the claim in an action in personam (referred to in this subsection as the relevant person) was, when the cause of action arose, the owner or charterer of, or in possession or in control of, the ship, an action in rem may (whether or not the claim gives rise to a maritime lien on that ship) be brought in the High Court against —

(i) that ship, if at the time when the action is brought the relevant person is either the beneficial owner of that ship as respects all the shares in it or the charterer of that ship under a charter by demise; or

(ii) any other ship of which, at the time when the action is brought, the relevant person is the beneficial owner as respects all the shares in it.<sup>58</sup>

#### **IV. The Present and Future of Straight Paper Based and Electronic Bills of Lading as Collateral**

##### **A. Security in Commercial Letter of Credit and Supply Chain Financing**

When one takes into account the above-discussed judicial and statutory clarifications on the legal nature of the straight bill of lading as a document of title, especially when issued by ship owners and fully-fledged (not contractual) carriers, it becomes apparent that they can serve as safe and useful collateral especially when secured creditors wish to limit the negotiation of the bills of lading by restricting their transfer only to designated parties.

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<sup>58</sup> The High Court (Admiralty Jurisdiction) Act, (2000), Chap. 123, 4 S.L.R. 156, § 4(4)(a)(b)(i)(ii) (Mode of exercise of admiralty jurisdiction), available at [http://statutes.agc.gov.sg/non\\_version/cgi-bin/cgi\\_retrieve.pl?&actno=Reved-123&date=latest&method=part](http://statutes.agc.gov.sg/non_version/cgi-bin/cgi_retrieve.pl?&actno=Reved-123&date=latest&method=part) [hereinafter the High Court (Admiralty Jurisdiction) Act].

Yet, bills of lading, whether negotiable or straight, have lost their appeal as collateral for many letter of credit bankers.<sup>59</sup> They only wish to act as paymasters of their issued or confirmed letters of credit and not as trade financiers. In addition, they find it too costly and risky to engage in a careful examination of the strict compliance of bills of lading which are increasingly populated by ambiguous “boxes”, “data fields”, “notations”, signatures, authentications, disclaimers and so on. Thus, they have migrated to a form of financing known as “supply chain financing.”<sup>60</sup> In this form of financing, “B” the banker provides cash payments to suppliers of goods in the distribution “chain” by purchasing or discounting the suppliers’ accounts receivable. Assume, for example, that “H”, a Honduran cooperative of fishermen, has a steady clientele for its lobsters among the United States importer-distributors of lobsters (“I”). If B purchases H’s accounts (usually payable on a 30 to 90-day basis) it will give H cash on a “non-recourse” basis and will assume the commercial risk of I’s non-payment. If B discounts H’s accounts, it will often do it on a “recourse” on the transferor of the account, *i.e.*, H will remain responsible for paying for the face amount of the accounts to B if I fails to pay for it. Thus, either in a purchase or discount transaction, H does not have to wait 30, 60, 90 or more days to use most of the amount owed by I.

To secure repayment of what it advanced or paid to H, B files for a security interest in H’s lobster inventory and accounts receivable owed by I so that they serve as collateral. This security interest will be recorded in the Honduran registry of secured transactions and will protect B against all claims secured and unsecured on that collateral provided that the filing is entitled to the requisite legal priority.<sup>61</sup> Concomitantly, B or its correspondent in the United States (“C”) extends a line of credit to I that will facilitate its payment of the accounts receivable owed to H. This line of

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<sup>59</sup> See Kozolchyk, *supra* note 52 (discussing a series of ICC Banking Commission Opinions that did away with UCP 500 dichotomy between FIATA multimodal transport bill of lading and port-to-port bill of lading and actual carrier v. contractual carrier, thereby eroding bill of lading holders’ protections, namely the ability of the applicant and issuing bank to recover against carriers and freight forwarders on cargo claims and to subject vessels to arrests and attachments); Kozolchyk, *supra* note 11, at 161–62, 240–41.

<sup>60</sup> See generally Kitt Carswell, *Supply Chain Financing: A new way for trade banks to strengthen customer relationships* (CGI Group Inc., White Paper, 2007), available at [http://www.cgi.com/files/white-papers/cgi\\_whpr\\_74\\_supply\\_chain\\_financ\\_e.pdf](http://www.cgi.com/files/white-papers/cgi_whpr_74_supply_chain_financ_e.pdf).

<sup>61</sup> See Decreto No. 182 de 2009, [the Honduran Law of Secured Transactions], [Article 50], La Gaceta, Diario Oficial de la República de Honduras, Jueves 28 de 2010 (Hond.). This law was the first in Latin America to successfully implement both the OAS Inter-American Model Law on Secured Transactions of 2002 and the 2009 Model Registry Regulations.

credit will be secured by I's inventory of lobsters, as well as with accounts receivable owed to I by restaurants, or (if I is a chain of restaurants) by I's own accounts receivable (including the credit card receipts of its consumers).

### **B. A Possible Use of Commercial or Standby Letters of Credit**

Notice that, in the simple purchase or discount of the respective set of accounts receivable, H and I saved themselves the costs of issuing, advising, confirming, negotiating and paying letters of credit. Yet, unless B is the same bank in Honduras and the United States it will have to enter into a (contractual) correspondent or line of credit relationship with its foreign correspondent. It is very likely that the need for supply chain financing will grow as developed nations continue to consume increasingly large amounts of raw materials and vegetables (among other products) from developing nations. It would not be unusual, then, if importers in developed nations would pressure their banks to facilitate their imports by purchasing accounts receivable and documents of title from such producers-exporters and their banks. Yet, the banks of the producers-exporters who do not have correspondent banking relationships with the importers' banks may well be persuaded to sell their accounts and documents of title if the banks of producers-exporters have the latter's firm assurance of purchase and that assurance is issued in advance of the tender of the specified accounts and/or of the documents of title, as is customary with commercial and standby letters of credit.<sup>62</sup>

The firmness and "abstraction" or independence from the equities and defenses stemming from underlying transactions, which are typical with commercial and standby letters of credit, would be an essential pre-requisite for the reassurances of certain payment or reimbursement needed between or among these supply chain financing "strangers." It is true that the banks that participate in a supply chain financing relationship could stipulate in their individual agreements that courts should interpret their contractual undertakings to each other as abstract and "final" undertakings. Yet, many countries enforce such undertakings only if they are sanctioned by treaty,

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<sup>62</sup> The situation would not be much different from that which took place during the Second World War with respect to highly scarce Spanish and French wines in the United States and Latin America. As described to the author by a Spanish banker, his bank used to receive "dozens of letters of credit" each day issued by banks in the United States and Latin America that would be payable against the presentation of invoices and shipping documents documenting the shipment of Spanish wines at prices with "approximate" ranges and with certain generic designations and certificates of quality.

statutory or customary laws.<sup>63</sup> In addition, the international customary law of letters of credit contains tried and tested binding rules on the time and manner in which correspondent banks pay and reimburse each other. Finally, a standby letter of credit known as “financial” can be paid in a very expeditious fashion when the examination of its documents is limited to checking that the exact or literal *haec verba* text of documents, especially certifications, specified in the letter of credit has been submitted by the beneficiary of the letter of credit. This diminishes not only the time of the issuing or confirming bank’s examination of the document but also reduces significantly the cost and risk of such an examination.

### C. The U.C.C. Article 5 and Article 9: "Financial" Letters of Credit and Supply Chain Financing

The combination of the law of letters of credit contained in Article 5 of the U.C.C. and of secured financing law in Article 9 of the same code with the International Standby Practices (ISP98), rules endorsed by the International Chamber of Commerce,<sup>64</sup> provides a safe, viable and cost-effective means to finance supply chain transactions by means of standby letters of credit and the appropriate filings of security interests in inventory, accounts receivable and their proceeds. UCC Article 9-inspired substantive

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<sup>63</sup> See the United Nations Commission on International Trade Law [UNCITRAL], *Explanatory note by the UNCITRAL secretariat on the United Nations Convention on Independent Guarantees and Stand-by Letters of Credit*, ¶¶ 3, 17, U.N. Doc. A/CN.9/431 (July 4, 1996), available at <http://www.uncitral.org/pdf/english/texts/payments/guarantees/guarantees.pdf>; See also Boris Kozolchyk, *Bank Guarantees and Letters of Credit: Time for a Return to the Fold*, 11 U. PA. J. INT'L BUS. L. 1, 14–15, 25–26 (1989), available at [http://www.law.upenn.edu/journals/jil/articles/volume11/issue1/Kozolchyk11U.Pa.J.Int'LB us.L.1\(1989\).pdf](http://www.law.upenn.edu/journals/jil/articles/volume11/issue1/Kozolchyk11U.Pa.J.Int'LB us.L.1(1989).pdf).

The widespread use of the term bank guarantee did not assure uniformity of legal treatment. To begin with, serious differences in substantive law on whether guarantees were abstract or causal obligations existed among jurisdictions involved. These differences were known to the draftsmen of the URCG who preferred to leave the determination of abstraction to courts or arbitral tribunals. . . . Most jurisdictions, however, lacked statutory rules on abstract guarantees. Instead, code and statutory rules on guarantees were essentially causal. In addition, courts in some of the most influential jurisdictions did not sanction abstract bank guarantees for internal trade until the mid-1970s or early 1980s. European banks, therefore, had to rely on contractual and customary law as the basis for enforcing bank guarantees, and hope that courts would remain sensitive to the need to enforce such a guarantee.

<sup>64</sup> See generally International Chamber of Commerce, *The International Standby Practices (ISP98)*, ICC Publication No. 590 (Jan. 1, 1999).



laws of secured transactions provide an effective filing and notice system, while “financial” standby letters of credit provide reliable assurances of payment and reimbursements between or among the banks financing these transactions. Indeed, the following hypothetical transaction illustrating the commercial utility of straight bills of lading serving as collateral could take place under the aegis of U.C.C. Article 9 and Guatemala’s and Honduras’ secured transactions laws:

As part of his line of credit with bank “IB”, Importer “I” in the United States procures the issuance of a financial standby letter of credit in favor of exporter “H” in Honduras. As confirmed by a confirming bank CB in Honduras, this letter of credit is made payable at sight against the presentation of, among other documents, one or more electronic invoices (accounts receivable) issued by H but conveyed as security to either CB or to IB or both. By conveying H’s accounts to CB or IB, they would become “owners” of these accounts. As noted earlier, this ownership is not a requirement of secured transactions law; but to avoid the inclusion of the accounts receivable in the estate of the bankrupt, U.S. law requires that there be evidence of ownership of the accounts by a purchaser who buys them outright and without recourse on the seller.<sup>65</sup> This conveyance would be accompanied by the issuance of straight bills of lading consigned to IB. A straight bill of lading is the most advisable because anybody who possesses one original of the negotiable bill of lading may claim delivery and defeat the bank’s security interest in the document of title under UCC § 9-331 and § 7-502 and counterpart provisions in UCC Article 9-influenced statutory law.

From the moment IB issued its standby letter of credit, it would file a security interest in the United States in I’s inventory and accounts derived from the above-mentioned sales to I’s customers. Similarly, CB would file a security interest in H’s inventory of lobsters and in its accounts receivable and proceeds in Honduras.

Upon determining the facial, *haec-verba* compliance of the documents submitted by H, CB would pay H the value of its

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<sup>65</sup> See 11 U.S.C. § 541 (Property of the estate) (2007) [United States Bankruptcy Code].

purchased or discounted accounts. H would then forward the invoices and straight bill of lading to IB. In some jurisdictions this could be done presently in an electronic manner; in others it will be possible to do so in the near future. As discussed earlier, unlike a negotiable bill of lading, the straight bill enables IB as its consignee to be the only claimant of the goods from the carrier, provided it presents such a straight bill of lading. This feature precludes anyone else from claiming the goods from the carrier. If the straight bill of lading consigned to IB is in electronic format, it would obviously arrive sooner at the counters of IB and would enable an earlier reimbursement and continuous credit extension.<sup>66</sup>

Thanks to the work of the National Law Center for Inter-American Free Trade (NLCIFT), including that of its project coordinator Dr. Marek Dubovec, research attorney Cristina Castaneda, software engineer Thomas Ose and the financial support of the Millennium Challenge Corporation, and in collaboration with the Millennium Challenge Account – Honduras and the Tegucigalpa Chamber of Industry and Commerce officials and technicians, Honduras has become the model for other developing nation registries in Latin America, Africa and Asia.<sup>67</sup> Given his involvement with the design of the Honduran registry and his dual common and civil law expertise in secured transactions law, the author asked Dr. Dubovec to comment on the feasibility of the above-described transaction. The following are his comments:

In Honduras and the United States, there are three options for the banks (IB and CB) to obtain a security interest in the goods: 1) taking possession of negotiable bills of lading or filing against the bill of lading; 2) being named on the straight bill of lading as the consignee, transferee or assignee; and 3) filing against the goods. If the IB in either country utilized any of these three options, it would perfect a security interest in the goods such as under UCC § 9-312 and § 9-313

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<sup>66</sup> For text of the Guatemalan and Honduran secured transaction laws that make possible the use of electronic documents of title, *See* National Law Center for Inter-American Free Trade, Interam<sup>SM</sup>Database, <http://natlaw.com/interam/> (last visited Mar. 21, 2011).

<sup>67</sup> Dr. Dubovec is a former graduate student and presently a colleague at the NLCIFT where he is the coordinator of secured transactions projects. Dr. Dubovec also teaches a course on UCC Article 9 at the James E. Rogers College of Law at the University of Arizona.

and Articles 33 and 34 of the Honduran Law on Secured Transactions. The first option (taking possession of the negotiable bill of lading) has the risks you pointed out, *i.e.*, anybody who possesses one original of the negotiable bill of lading may claim delivery and defeat the bank's security interest in the document of title under UCC § 9-331 and § 7-502. In addition, the security interest will remain temporarily perfected only for 20 days after delivery under § 9-312. The problem with this option is the time limit imposed on the security interest – it starts out when the document naming the bank as the consignee is issued and terminates 20 days after delivery. It does not protect the creditor (IB) prior to the issuance of the document and following the expiration of the 20-day period.

The second option (being named as the consignee on a straight bill of lading) would protect the bank, as you pointed out, against deceptive delivery to a third party. In addition to ensuring the security of delivery, the bank would also have a perfected security interest. However, once the goods are released, the straight bill of lading ceases to have any effects and the creditor has the same problem as faced by the person who took possession of the negotiable bill of lading. The security interest will remain temporarily perfected for 20 days under § 9-312. The problem with this option is the time limit imposed on the security interest – it starts out when the document naming the bank as the consignee is issued and terminates 20 days after delivery. It does not protect the creditor (the issuing bank) prior to the issuance of the document and following the expiration of the 20-day period. The second option provides the same protection as regards the security interest and its priority as the negotiable bill of lading. The option seems to be superior to the negotiable bill of lading with respect to security of delivery.

The third option (filing as to the goods or inventory and accounts which in many jurisdictions automatically attaches to proceeds) would combine with the others to provide a more complete and longer-term protection for the secured creditor. As soon as the importer walks into the bank's office and requests the issuance of a letter of credit, the bank should request an authorization under UCC § 9-509 to file a

financing statement against the importer that would include his inventory and accounts. The collateral should be described as inventory and accounts. Only then should the issuance of the letter of credit alone or in combination with a line of credit be approved. The bank can thus obtain priority and protection against third party claims long before the goods are loaded on board the vessel and a bill of lading issued. If, subsequently, a negotiable bill of lading were issued and negotiated to a third party, the third party's claim would have priority over the previously-perfected security interest of the bank under UCC § 7-503. However, if the bank makes sure that only a straight bill of lading is issued, nobody can defeat the bank's security interest. The bank's security interest will be perfected for 5 years or until expiration of the registration, not merely for 20 days.

## **V. Conclusions and Recommendations**

*Carewins* and *The Rafaela* have made it possible to deal with straight bills of lading as documents of title in English and Commonwealth laws and also as reliable collateral, except when issued by some freight forwarders. Articles 1, 5, 7 and 9 of the U.C.C. and their counterparts in an increasing number of Latin American countries, as well as UCP600 and ISP98, now make it possible for banks to rely on: (1) paper-based or electronic straight bills of lading, accounts receivable and goods and proceeds thereof covered by them as collateral for supply chain financing; and (2) the more certain enforcement of irrevocable and abstract forms of promises of payment and reimbursements between or among the participating banks. The time is approaching when banks that engage in supply chain financing should avail themselves of these joint capabilities. The statutory and treaty basis for such capability exists. The International Chamber of Commerce should consider the promulgation of best practice customary rules involving the use of standby financial letters of credit in supply chain financing worldwide.

**The Road to Nowhere:  
*Caterpillar v. Usinor* and CISG Claims by Downstream Buyers Against  
Remote Sellers**

Donald J. Smythe\*

**Introduction**

The first issue to resolve in any contract dispute is which body of contract law applies. The task is not as simple as it sounds or as it once was. In an international contract dispute the court must first apply private choice of law rules to determine which nation-state's laws govern. If the court determines that U.S. law applies it must then decide which body of U.S. law. There are a hundred and one different sets of contract rules that could apply to an international contract dispute under U.S. law alone. If the parties have places of business in different Contracting States and the contract is for goods for non-household uses then the UN Convention on Contracts for the International Sale of Goods ("CISG", "the Convention") applies under federal law.<sup>1</sup> If the parties do not have places of business in different contracting states and the contract is for non-household goods, or if the parties do have places of business in different Contracting States and the contract is for household goods, then some U.S. state's version of Article 2 of the Uniform Commercial Code (UCC) will apply.<sup>2</sup> If the contract is not for goods of any kind then some state's version of the common law will

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<sup>1</sup> See United Nations Convention on Contracts for the International Sale of Goods art. 1(a), Apr. 11, 1980, S. TREATY DOC. NO. 98-9 (1983), 1489 U.N.T.S. 3, available at <http://www.cisg.law.pace.edu/cisg/text/treaty.html> [hereinafter CISG]. The U.S. Senate ratified the CISG in 1986 giving it the force of federal law when the Convention came into effect on January 1, 1988. See also *BP Oil Int'l, Ltd. v. Empresa Estatal Petroleos de Ecuador (PetroEcuador)*, 332 F.3d 333, 336 (5th Cir. 2003) ("The CISG, ratified by the Senate in 1986, creates a private right of action in federal court."). As of January 20, 2010 a total of 74 nations have ratified the CISG and thus become "Contracting States." See Pace Law School Institute of International Commercial Law, CISG: participating countries (Jan. 22, 1998), <http://www.cisg.law.pace.edu/cisg/countries/cntries-United.html>.

<sup>2</sup> In some Contracting States the CISG might apply even if the parties do not have places of business in different Contracting States under CISG, Article 1(b). The U.S. has, however, declared a reservation to Article 1(b) as permitted by CISG, Article 95. Thus, Article 1(b) does not apply under U.S. law. See U.S. Ratification of 1980 United Nations Convention on Contracts for the International Sale of Goods, 52 Fed. Reg. 6262-02 (March 2, 1987) [hereinafter U.S. Ratification of CISG] ("United States ratification was coupled with a declaration that the United States would not be bound by Article 1(1)(b), which will have a narrowing effect on the sphere of application of the Convention.").

apply.<sup>3</sup> Since there are fifty states this adds up to a hundred and one different sets of contract rules that could apply to the parties' dispute.

In the modern world, with its growing volume of transnational transactions this is too many rules. Indeed, the purpose of the CISG is to promote uniformity in international sales law and good faith in international trade.<sup>4</sup> Although the CISG itself only seeks to bring uniformity to a limited set of international contracts, it was the product of larger forces to bring harmony and uniformity to international law and facilitate the expansion of international trade and commerce.<sup>5</sup> It is important to remember that the CISG was the product of a bargain between representatives from many nations with a diverse range of legal systems. As a consequence, the CISG's rules are quite spare by comparison to U.S. law and they are stated in unfamiliar language that is devoid of many U.S. commercial law terms. The spare structure of the CISG's rules and the unfamiliar terms inevitably raise questions of interpretation. What are courts to do when they face questions that the CISG does not explicitly address, at least in terms with which they are familiar?

The CISG itself offers some guidance on this question: Under Article 7(1) courts are directed to interpret the CISG's provisions in a manner that promotes uniformity in its application and good faith in

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<sup>3</sup> In some cases it may be difficult to determine whether the contract is for goods or services. Both the CISG and U.S. case law apply a test for determining whether the contract should be treated as one for the sale of goods. The majority of courts in the U.S. apply the predominant factor test under domestic law. *BMC Industries, Inc. v. Barth Industries, Inc.*, 160 F.3d 1322, 1330 (11th Cir. 1998). This approach is similar to the test applied under the CISG, Article 3(2). See Explanatory Note by the UNCITRAL Secretariat on the Convention on the Limitation Period in the International Sale of Goods and the Protocol amending the Convention on the Limitation Period in the International Sale of Goods, ¶ 7, U.N. Doc. V.89-53886 (June 1989):

Since the Convention applies only in respect of international sales contracts, it clarifies whether contracts involving certain services are covered. A contract for the supply of goods to be manufactured or produced is considered to be a sales contract unless the party who orders the goods undertakes to supply a substantial part of the materials necessary for their manufacture or production. Furthermore, when the preponderant part of the obligations of the party who furnishes the goods consists in the supply of labor or other services, the Convention does not apply.

<sup>4</sup> See CISG, *supra* note 1, preamble & art. 7(1).

<sup>5</sup> See Gunther A. Weiss, *The Enchantment of Codification in the Common-Law World*, 25 YALE J. INT'L L. 435, 445 (2000).

international trade.<sup>6</sup> Article 7(2) indicates that when confronted with an apparent gap in the CISG, courts must first look to the general principles upon which the CISG is based and, if they fail to find any, then select the domestic legal rules applicable under private choice of law rules.<sup>7</sup> Unfortunately, this invites controversy. It encourages parties to find gaps in the rules so that they may argue for the application of domestic laws that work to their advantage. To the extent that courts are susceptible to these arguments, the scope of the CISG is narrowed and diverse domestic laws displace uniform international laws in the adjudication of international sales disputes. The purpose of the CISG is thus undermined.

The problem is vividly illustrated by a recent U.S. federal district court case in the Northern District of Illinois: *Caterpillar v. Usinor*.<sup>8</sup> *Caterpillar* addresses a fundamental contracting problem: whether a downstream buyer – a buyer who bought goods from a remote seller through some intermediary – can make a contract claim against a remote seller – a seller who sold goods to a downstream buyer through some intermediary. The court in *Caterpillar* thus had an opportunity to contribute to the development of a coherent body of international sales law and promote good faith in international trade. It did exactly the opposite. The court accepted an argument that the preemptive effect of the CISG was limited to contract claims by the seller's immediate buyer and construed the CISG to require privity. It also allowed the downstream buyer to make a domestic contract claim against the remote seller under the common law doctrine of promissory estoppel. Part I of this essay provides a Statement of the Case. Part II, the Analysis Section, argues that the court succumbed to an overwhelming "homeward trend bias" and rendered an opinion that undermines the CISG and confounds Illinois law. Part II further argues that the court could and should have reached the same outcome by developing a theory for allowing downstream buyers to make claims against remote sellers under the CISG.

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<sup>6</sup> CISG, *supra* note 1, art. 7(1) ("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 international trade.").

<sup>7</sup> *Id.* art. 7(2) ("Questions concerning matters governed by this Convention which are not expressly settled in it are to be settled in conformity with the general principles on which it is based or, in the absence of such principles, in conformity with the law applicable by virtue of the rules of private international law.").

<sup>8</sup> *Caterpillar, Inc. v. Usinor Industeel*, 393 F. Supp. 2d 659 (N.D. Ill. 2005).

## I. Statement of the Case

### A. A Fork in the Road

The case arose from a set of transactions that Caterpillar undertook to supply its customers with mining trucks at various locations in the U.S.<sup>9</sup> To that end, Caterpillar negotiated with Usinor Industeel (“Usinor”), a French steel company, and its own Mexican subsidiary, Caterpillar, Mexico (“CMSA”) for the supply of steel to CMSA so that CMSA could use the steel in the manufacture of the truck bodies.<sup>10</sup> Usinor represented to Caterpillar and CMSA that its steel was of a new type called “Creusabro 8000” which was harder, stronger, welded better, and could be processed more cheaply than regular steel.<sup>11</sup> In fact, Usinor even supplied Caterpillar with a sample of the steel and indicated that the sample was representative of the steel they could provide in substantial quantities.<sup>12</sup> Caterpillar informed Usinor that the steel would be used for truck bodies and gave Usinor the design specifications.<sup>13</sup>

Based on these representations from Usinor, Caterpillar submitted proposals to its customers to manufacture dump trucks using the Creusabro steel.<sup>14</sup> After contracting to supply trucks to many of its customers, Caterpillar contracted with CMSA for the supply of truck bodies and CMSA contracted with Usinor for the supply of Creusabro steel.<sup>15</sup> Caterpillar subsequently delivered new trucks to its customers. There were apparently no problems with the trucks delivered in the first shipment, but the bodies in several of the trucks delivered in subsequent shipments cracked.<sup>16</sup> The cracks and potential for cracking made the vast majority of the trucks that Caterpillar delivered to its customers inoperable.<sup>17</sup> In

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<sup>9</sup> The transactions were actually initiated by Usinor Idusteel and its North American subsidiary, Usinor Industeel, USA, who were defendants in the case. They initially requested a meeting with Caterpillar to present a sales pitch for Usinor’s new “Creusabro” steel. *Caterpillar*, 393 F. Supp. 2d at 664–65.

<sup>10</sup> This explanation of the commercial dispute is a simplification. Caterpillar also contracted for truck bodies manufactured with the Creusabro steel from an independent company called Western Technology Services International, Inc. (Westech). The truck bodies manufactured by Westech had the same defects as those manufactured by CMSA. *Id.*

<sup>11</sup> *Id.*

<sup>12</sup> *Id.* at 665.

<sup>13</sup> *Id.*

<sup>14</sup> *Id.*

<sup>15</sup> *Caterpillar*, 393 F. Supp. 2d at 665.

<sup>16</sup> *Id.* at 666.

<sup>17</sup> *Id.*



addition, the steel proved to be of low quality and more difficult to use than CMSA had been led to believe it would be so CMSA incurred higher than expected costs in manufacturing the truck bodies.<sup>18</sup>

### *B. The Road Taken*

Caterpillar and CMSA filed a complaint against Usinor seeking damages for repairs to cracked truck bodies, increased production costs, and loss of goodwill.<sup>19</sup> The complaint alleged breach of express and implied warranties under the CISG as well as the Illinois version of Article 2 of the UCC, in addition to a promissory estoppel claim under Illinois common law.<sup>20</sup> In its defense, Usinor claimed, among other things, that all of Caterpillar's and CMSA's UCC claims were preempted by the CISG, and that since the CISG states that it governs only the formation of the contract of sale and the rights and obligations of the seller and buyer, only CMSA had standing to assert any claims.<sup>21</sup>

The case thus raised a question about the preemptive effect of the CISG. Since the CISG is federal law, the court correctly observed that this was essentially a question about the CISG's scope.<sup>22</sup> Under the Supremacy Clause of the U.S. Constitution the CISG clearly preempts any state law causes of action within its scope.<sup>23</sup> Caterpillar argued that the CISG could only preempt state law claims by CMSA.<sup>24</sup> The court did not directly address this issue. Instead, in a subtle but important way, the court shifted the framing of the question from one about the preemptive effect of the CISG to one about standing to bring claims under the CISG.<sup>25</sup> The court

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<sup>18</sup> *Id.*

<sup>19</sup> The complaint also named Usinor's North American distributor, Leeco Steel Products, Inc. (Leeco) and its North American subsidiary Usinor Industeel, Inc. (Usinor USA). *Id.* at 667. The counts filed against Leeco and Usinor USA were in the alternative to the counts filed against Usinor in the event that Leeco and Usinor USA were found not to be Usinor's agents. Since the court did find that Leeco and Usinor USA were Usinor's agents these alternative counts were dismissed. *Id.* at 672.

<sup>20</sup> *Id.* at 667. There was also a claim under French law in the alternative to the application of U.S. law but the court dismissed that claim as well. *Id.* 669.

<sup>21</sup> *Id.*; see CISG, *supra* note 1, art. 4 (stating that the CISG governs "only the formation of the contract of sale and the rights and obligations of the seller and buyer arising from such a contract.").

<sup>22</sup> *Caterpillar*, 393 F. Supp. 2d at 667.

<sup>23</sup> *Id.*

<sup>24</sup> *Id.*

<sup>25</sup> See *id.* at 673–74. The court in *Caterpillar* interprets Article 4 of the CISG to limit claims to those by the buyer against the seller. *Id.* at 674. But Article 4 indicates that the CISG governs only the "rights and obligations of the seller and buyer." CISG, *supra* note 1,

noted that it was CMSA that bought the steel from Usinor, not Caterpillar, and that only CMSA could therefore assert claims against Usinor under the CISG.<sup>26</sup> Since Caterpillar was not a party to the contract between CMSA and Usinor, Caterpillar did not have standing to bring claims against Usinor under the CISG and the CISG did not therefore preempt Caterpillar from bringing state law claims against Usinor.<sup>27</sup> As the discussion below will elaborate, this was an unfortunate error in the court's logic.

Caterpillar made UCC claims against Usinor for breach of express and implied warranties as well as a promissory estoppel claim under Illinois common law.<sup>28</sup> Illinois law however, requires privity of contract for the recovery of economic damages under UCC express or implied warranty claims.<sup>29</sup> Caterpillar attempted to establish that certain exceptions to the privity requirement applied, but the court disagreed.<sup>30</sup> Caterpillar was thus left with only its promissory estoppel claim. Under Illinois law a plaintiff can assert a promissory estoppel claim by alleging that (i) an unambiguous promise was made, which was (ii) reasonably and justifiably relied upon by the promisee, that (iii) the reliance was expected and foreseeable by the promisor, and that (iv) the promisee relied to her detriment.<sup>31</sup> Usinor argued that none of the statements it had made to Caterpillar constituted unambiguous promises since they were merely representations of fact and opinion, and that Caterpillar's promissory estoppel claim should therefore have been dismissed too.<sup>32</sup> The court, however, again disagreed. The court therefore allowed CMSA to proceed with CISG claims against Usinor but not with any Illinois UCC or common law claims, and it disallowed Caterpillar from proceeding with any CISG claims or Illinois UCC claims but allowed it to proceed with an Illinois common law promissory estoppel claim. This confounded both the CISG and Illinois law.

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art. 4. It does not state that the CISG limits claims to those by the immediate buyer against the seller or that it precludes claims by downstream buyers against upstream sellers. *Id.*

<sup>26</sup> *Caterpillar*, 393 F. Supp. 2d at 674. This conclusion presumes, of course, that under the CISG a seller can only have obligations to a party with which it is in privity of contract. That is not at all clear. See Ingeberg Schwenzer and Mareike Schmidt, *Extending the CISG to Non-Privity Parties*, 13 VINDOBONA J. OF INT'L COM. L. & ARB. 109, 114–15 (2009) (contending that just because the CISG is silent regarding third-party claims against sellers does not mean that it precludes such claims).

<sup>27</sup> *Caterpillar*, 393 F. Supp. 2d at 673–76.

<sup>28</sup> *Id.* at 667.

<sup>29</sup> *Id.* at 677–78.

<sup>30</sup> *Id.* at 678.

<sup>31</sup> *Id.* at 679–80.

<sup>32</sup> *Id.* at 680–81.

## II. Analysis

This section argues that the *Caterpillar* court's opinion undermines efforts to unify international commercial law. It argues that the court should have interpreted the CISG to preempt any domestic contract laws, including the UCC and the doctrine of promissory estoppel. It argues that, by allowing domestic contract claims, the *Caterpillar* court failed to promote good faith in international trade or make any effort to apply the CISG in conformity with the general principles upon which it is based. Moreover, it argues that the court confounded both the CISG and Illinois law when it construed the CISG to require privity of contract for a breach of contract claim and allowed a domestic contract claim against the remote seller under the common law doctrine of promissory estoppel. If followed, *Caterpillar* will not only create disunity in international sales, impede good faith in international trade, and promote forum shopping, but it will also diminish the amount and value of information remote sellers provide about their goods and distort their decisions about their distribution systems. Finally, this section proposes an alternative approach: courts should instead construe the CISG to preempt all domestic contract claims and find a way of allowing downstream buyers to make claims against remote sellers under the CISG itself. The CISG can be construed to allow downstream buyers to make claims against remote sellers under Article 16(2)(b), a provision that is similar to the common law doctrine of promissory estoppel.

### A. *This is the Road to Nowhere: Problems with the Caterpillar Decision*

To begin with, the *Caterpillar* court construed the scope of the CISG too narrowly. Indeed, the court misapplied Article 4 of the CISG when it construed the preemptive effect of the CISG to extend only so far as the CISG confers standing on a party to bring a cause of action. On the contrary, since the CISG is federal law its preemptive effect extends to any matters within its scope. Although Article 4 states that the CISG governs only the "formation of the contract" and the "rights and obligations of the seller and buyer," this should at the very least mean that the CISG governs all the contractual rights and obligations of the seller and buyer and that it therefore preempts any conflicting domestic contract laws that might otherwise apply.<sup>33</sup> As the court construed the case in *Caterpillar* there was a

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<sup>33</sup> Article 4 also states that the CISG is "not concerned with: (a) the validity of the contract or of any of its provisions or of any usage; (b) the effect which the contract may have on the property in the goods sold." CISG, *supra* note 1, art. 4(a). Neither of these limitations seems relevant to the scope of a seller's obligations.

contract between CMSA and Usinor for the supply of steel. This contract was clearly governed by the CISG. Thus, any contractual obligations that Usinor might have had towards a third party such as Caterpillar should have derived from the provisions of the CISG.<sup>34</sup> As the discussion below will elaborate, the court might have found such obligations elsewhere in the CISG if it had looked for them, but it did not.

Indeed, as the court construed the case there was a separate contract between Caterpillar and CMSA for the supply of truck bodies.<sup>35</sup> This contract was also clearly governed by the CISG, since Caterpillar and CMSA had places of business in different Contracting States.<sup>36</sup> The CISG should therefore have preempted any domestic contract laws that might otherwise have applied to their transaction, including the UCC as well as Illinois common law doctrines, such as promissory estoppel, which sound in contract rather than property or tort. Thus, all the contractual rights and obligations of both Caterpillar and CMSA should have derived from the provisions of the CISG. It may be difficult to imagine which provisions of the CISG may be construed to endow a buyer with rights against a third party, such as a remote seller, but even if the CISG does not endow the buyer with such rights, that does not justify the court in allowing the buyer to assert claims under domestic contract law.

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<sup>34</sup> This is the way other federal courts have construed the preemptive effect of the CISG. See *Geneva Pharm. Tech. Corp. v. Barr Laboratories, Inc.*, 201 F. Supp. 2d 236, 285 (S.D.N.Y. 2002) (“This Court concurs that ‘the expressly stated goal of developing uniform international contract law to promote international trade indicates the intent of the parties to the treaty to have the treaty preempt state law causes of action.’”); *Asante Tech., Inc. v. PMC – Sierra, Inc.*, 164 F. Supp. 2d 1142, 1151 (N.D. Cal. 2001) (“The Court concludes that the expressly stated goal of developing uniform international contract law to promote international trade indicates the intent of the parties to the treaty to have the treaty preempt state law causes of action.”).

<sup>35</sup> *Caterpillar*, 393 F. Supp. 2d at 677. One of the puzzles in the case is why Caterpillar did not attempt to rely on principles of agency to contend that it was a party to the contract with Usinor for the supply of the steel. Perhaps the plaintiff’s strategy was to expand the scope of its claims. CMSA was clearly precluded from making domestic law claims and Caterpillar would have been too if it was a party to the contract for the supply of the steel. As a separate party contracting for the supply of the truck bodies, however, Caterpillar could plausibly attempt to make domestic law claims.

<sup>36</sup> See CISG, *supra* note 1, art. 1(a). Article 1(a) of the CISG states that it applies to contracts of sale between parties whose place of business are in different Contracting States. Since both the U.S. and Mexico had adopted the CISG before the contract was formed, they were both Contracting States. See Pace Law School Institute of International Commercial Law, Mexico (Jan. 22, 1998), <http://cisgw3.law.pace.edu/cisg/countries/cntries-Mexico.html>; Pace Law School Institute of International Commercial Law, United States (Jan. 22, 1998), <http://cisgw3.law.pace.edu/cisg/countries/cntries-United.html>.

The court in *Caterpillar* construed the question of whether a buyer under a CISG contract may have rights against a third party, such as a remote seller, as a matter not addressed by the CISG. This is a dubious construction of the CISG at best. Although Article 4 indicates that the CISG governs only the formation of the contract and the rights and obligations of the seller and buyer, this implies that once a contract has been formed under the CISG it should define all the contractual rights and obligations of the seller and buyer.<sup>37</sup> The CISG might not preempt claims under tort or property but it should preempt any claims under domestic contract law.<sup>38</sup>

By allowing domestic contract claims against Usinor even though it held the CISG applied, the court in *Caterpillar* reflected the “homeward trend bias” that the drafters of the CISG clearly hoped to avoid.<sup>39</sup> By construing the preemptive effect of the CISG narrowly the court gave broader effect to non-uniform domestic laws in a case where doing so favored the domestic party. One of the problems in interpreting an international convention such as the CISG, of course, is that there is no international equivalent of the common law.<sup>40</sup> Nonetheless, excessive recourse to domestic law in the face of apparent gaps in the CISG only

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<sup>37</sup> See CISG, *supra* note 1, art. 4 (“This Convention governs only the formation of the contract of sale and the rights and obligations of the seller and the buyer arising from such a contract.”); *Geneva Pharm.*, 201 F. Supp. 2d. at 285; *Asante Tech.*, 164 F. Supp. 2d at 1151.

<sup>38</sup> See CISG, *supra* note 1, art. 4.

<sup>39</sup> References to a homeward trend bias in CISG jurisprudence abound in the literature. See, e.g., LARRY DIMATTEO ET AL., INTERNATIONAL SALES LAW: A CRITICAL ANALYSIS OF CISG JURISPRUDENCE 2–3 (2005); JOHN O. HONNOLD, DOCUMENTARY HISTORY OF THE UNIFORM LAW FOR INTERNATIONAL SALES: THE STUDIES, DELIBERATIONS, AND DECISIONS THAT LED TO THE 1980 UNITED NATIONS CONVENTION WITH INTRODUCTIONS AND EXPLANATIONS 1 (1989); Harry M. Fletcher, *The Several Texts of the CISG in a Decentralized System: Observations on Translations, Reservations and Other Challenges to the Uniformity Principle in Article 7(1)*, 17 J.L. & COM. 187, 200–04 (1998). As the Guide to the CISG, Article 7 explains, “[I]t is especially important to avoid different constructions of the provisions of this Convention by national courts, each dependent upon the concepts used in the legal system of the country of the forum.” United Nations Commission on International Trade Law [UNCITRAL], Commentary on the Draft Convention on Contracts for the International Sale of Goods, Prepared by the Secretariat, ¶ 17, UN Doc. A/CONF.97/5 (Mar. 14, 1979), available at <http://www.globalsaleslaw.org/index.cfm?pageID=644#Article%201>.

<sup>40</sup> JOHN FELEMEGAS, AN INTERNATIONAL APPROACH TO THE INTERPRETATION OF THE UNITED NATIONS CONVENTION ON CONTRACTS FOR THE INTERNATIONAL SALE OF GOODS (1980) AS UNIFORM SALES LAW 10 (2007).

frustrates the CISG's purpose of promoting uniformity and encourages forum shopping.<sup>41</sup>

Article 7(1) states that the CISG should be interpreted with "regard" to its "international character" and "the need to promote uniformity in its application and the observance of good faith in international trade." Several scholars have argued that this requires courts to take a liberal approach to interpreting its provisions as a body of international law, rather than as the laws of the Contracting States.<sup>42</sup> Article 7(2) states that "questions concerning matters governed by [the CISG] . . . are to be settled in conformity with the general principles on which it is based". Commentators have argued that this suggests two interpretive methods: one involving an examination of the general principles on which the CISG is based, the other involving reasoning by analogy to other CISG provisions.<sup>43</sup> These are very broad tools, and even though the CISG may therefore appear to have many gaps, most commentators argue there is a mandate for national courts to fill the gaps and construct a body of international case law to support and supplement the provisions explicitly stated in the CISG.<sup>44</sup>

Some foreign courts have recognized this mandate.<sup>45</sup> Thus, in a case involving a buyer that made repeated, though perhaps sporadic, purchases over a two year period, a Finish court held that the seller had a duty to continue supplying beyond the terms of any discrete transaction because the buyer's "operations cannot be based on a risk of an abrupt ending of a

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<sup>41</sup> *Id.* at 11.

<sup>42</sup> See e.g., Michael Joachim Bonell, *General Provisions: Article 7*, in COMMENTARY ON THE INTERNATIONAL SALES LAW: THE 1980 VIENNA SALES CONVENTION 73 (C.M. Bianca & M.J. Bonell eds., 1987); Felemegas, *supra* note 40 at 11–12; Bruno Zeller, *The UN Convention on Contracts for the International Sale of Good – A Leap Forward towards Unified International Sales Laws*, 12 PACE INT'L L. REV. 79, 105–06 (2000).

<sup>43</sup> See e.g., Bonell, *supra* note 42, ¶ 2.3.2 ("The formula used in Article 7(2) is to be understood in a broad sense to cover not only recourse to, «general principles», but also reasoning from specific provisions by analogy. The two approaches should however not be confused, since they are complementary to each other and operate in a different manner."); JOHN O. HONNOLD, UNIFORM LAW FOR INTERNATIONAL SALES UNDER THE 1980 UNITED NATIONS CONVENTION 16–17 (4TH ED. 2009); Phanesh Koneru, *The International Interpretation of the UN Convention on Contracts for the International Sale of Goods: An Approach Based on General Principles*, 6 MINN. J. GLOBAL TRADE 105 (1997).

<sup>44</sup> See e.g., Bonell, *supra* note 42, ¶ 2.2.1 ("[T]he Convention . . . is intended to replace all rules in legal systems previously governing matters within its scope . . . . This means that in applying the Convention there is no valid reason to adopt a narrow interpretation.").

<sup>45</sup> See DIMATTEO ET AL., *supra* note 39, at 19–31 (discussing CISG methodology and jurisprudence).

contract.”<sup>46</sup> The court’s rationale was premised on interpreting the CISG to include a general “principle of loyalty” which requires the parties to “act in favor of a common goal” and “consider the interests of the other.”<sup>47</sup> In another case, an Austrian court held that the CISG authorized payment of interest as a part of the contract damages even though Article 74 of the CISG makes no mention of interest because of the general CISG principle that “full compensation” was required.<sup>48</sup> Here the court inferred the principle from other provisions of the CISG.<sup>49</sup> The point is not that the court in either case was necessarily correct, but that references to the general principles of the CISG and analogies to other CISG provisions have been used by courts in other Contracting States to fill gaps in the CISG.

The implication is that the CISG is much broader than its rather spare structure of rules and provisions would suggest, and its preemptive effect on any adopting nation’s domestic laws should be correspondingly greater. Indeed, at least some foreign tribunals have apparently heeded the admonishment in Article 7(2) to interpret the CISG in conformity with the general principles upon which it is based.<sup>50</sup> American courts should do the same. The court in *Caterpillar*, however, concluded that simply because the CISG did not explicitly address the question of whether a downstream third party has contract rights against a remote seller it was a matter to be decided under domestic law. The court thus not only misconstrued the preemptive effect of the CISG on the parties’ contract rights, it also failed to make any effort to apply the CISG in conformity with the general principles upon which it is based. This was hardly in concert with Article 7(1)’s directive to interpret the CISG with regard to its international character and the need to promote uniformity and good faith in international trade.

In fact, the decision in *Caterpillar* undermined principles of uniformity and good faith in international trade even more directly. The court’s decision implies that a remote seller under a CISG contract may

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<sup>46</sup> See *Plastic carpets case*, Helsingin hovioikeus [Helsinki Court of Appeals], Oct. 26, 2000, S 00/82 (Fin.), available at <http://cisgw3.law.pace.edu/cases/001026f5.html>; see also DIMATTEO, *supra* note 39, at 24–25 (stating that the Helsinki Court of Appeals held that a two-year business relationship justifies a duty of loyalty).

<sup>47</sup> *Id.*

<sup>48</sup> See *Rolled Metal Sheets (Austria v. F.R.G.)*, Internationales Schiedsgericht der Bundeskammer der gewerblichen Wirtschaft [Arbitral Trib. - Vienna] June 15, 1994, SCH-4318 (Austria), available at <http://www.cisg.law.pace.edu/cisg/wais/db/cases2/940615a4.html>.

<sup>49</sup> DIMATTEO ET AL., *supra* note 39, at 26–27.

<sup>50</sup> See *id.* at 19–31 (discussing CISG methodology and jurisprudence).

have contractual obligations to downstream third parties under domestic contract law. Usinor was found potentially liable to Caterpillar for a promissory estoppel claim.<sup>51</sup> In fact, if Illinois law did not have privity requirements for express and implied warranty claims under the UCC, Usinor would also potentially have been liable for breaches of UCC warranties. Many states do not have such privity requirements.<sup>52</sup> In those states the consequences of the court's narrow interpretation of the CISG would have exposed Usinor to an even wider range of domestic contract claims. The court's decision implies that the legal obligations of a seller in a CISG contract depend on whether the seller's buyer contracts with a third party in the U.S. and which state's laws apply to the contract. *Caterpillar* thus hardly promotes uniformity in international trade – even across states within the U.S.

Indeed, the domestic laws of some other Contracting states under the CISG also have privity requirements (or their equivalent) for at least some contract claims.<sup>53</sup> Thus, if courts in those nations follow *Caterpillar* and interpret the preemptive effect of the CISG narrowly, any contract breach of warranty claims under their domestic laws will be barred by the privity requirement. Moreover, many Contracting states do not allow actions for promissory estoppel or any equivalent foreign doctrine.<sup>54</sup> Thus, third parties

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<sup>51</sup> One could debate, of course, whether the doctrine of promissory estoppel properly belongs in contract, but it at least arguably creates contract-like obligations. U.S. courts have generally agreed. *See Geneva Pharm.*, 201 F. Supp. at 286 (“Breach of contract and promissory estoppel are ‘two sides of the same coin, and that coin is a cause of action for breach of contract.’”) (citing *Qatar Nat'l Navigation & Transp. Co. v. Citibank*, No. 89 Civ. 464 (CSH), 1998 WL 516117, at \*6–7 (S.D.N.Y. Aug. 20, 1998) (“Promissory estoppel is an equitable remedy, the asserted effect of which . . . is to estop [Citibank] from denying the existence of the contract pleaded.”); *Pitak v. Bell Atl. Network Servs.* 928 F. Supp. 1354, 1367 (D.N.J. 1996) (“Promissory estoppel is a cause of action related to breach of contract.”)).

<sup>52</sup> *See* JAMES J. WHITE & ROBERT S. SUMMERS, UNIFORM COMMERCIAL CODE 406 (5th ed. 2000) (“[T]he law permits a non-privity buyer to recover for direct economic loss if the remote seller has breached an express warranty. Where the buyer cannot show reliance on express representations by the remote seller, however, the case law is in conflict.”).

<sup>53</sup> Privity is a common law doctrine and so vestiges of the requirement remain in many common law nations. *See, e.g.*, Francis Dawson, *New Zealand Privity of Contract Bill*, 2 OXFORD J. LEGAL STUD. 448, 451, 453 (1982); Michael Trebilcock, *The Doctrine of Privity of Contract: Judicial Activism in the Supreme Court of Canada*, 57 U. TORONTO L.J. 269, 269–70 (2007).

<sup>54</sup> European courts in civil law systems, for instance, do not recognize the doctrine of promissory estoppel and generally do not allow as many gratuitous promises to be enforced as U.S. courts. *See, e.g.*, HEIN KOTZ & AXEL FLESNER, EUROPEAN CONTRACT LAW 76–77 (Tony Weir trans., 1997).



like Caterpillar might have no recourse under their domestic contract laws against a remote seller like Usinor. If followed, *Caterpillar* could thus establish a system under which American third parties such as Caterpillar might be able to make domestic contract claims against CISG sellers like Usinor (depending on which state's laws applied), but similarly situated third parties in foreign Contracting States might not. This would undermine a basic principle of reciprocity and equal treatment.<sup>55</sup> *Caterpillar* is thus antithetical to good faith in international trade.

It may also promote forum shopping. There is a well-known homeward trend in the application of choice of law rules under private international law.<sup>56</sup> Suppose that Alpha, with place of business in Contracting State A, contracted for the sale of goods to an intermediary, Beta, with place of business in Contracting State B, who then contracted for the resale of the goods to Gamma, with place of business in Contracting State C. Suppose that State A's domestic laws included a privity requirement but State C's domestic laws did not. Suppose that Gamma wished to bring an action for breach of warranty against Alpha. Suppose there was enough flexibility in the choice of law rules to allow a court to apply its domestic laws and suppose courts were inclined to exhibit a homeward trend. Under *Caterpillar* Gamma would obviously prefer to file an action against Alpha in State C rather than in State A. Given the homeward trend in the application of choice of law rules, this would probably allow Gamma domestic actions against Alpha under the laws of State C that would be unavailable under the CISG or the laws of State A. Such forum-shopping would only exacerbate *Caterpillar's* tendency to promote disharmony in the application of the laws governing international sales.

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<sup>55</sup> The U.S. implied the need for reciprocity in the application of the CISG by declaring a reservation under CISG, Article 95 excluding the application of CISG, Article 1(b). See U.S. Ratification of CISG, *supra* note 2. By declaring a reservation against Article 1(b) the U.S. ensured that the CISG will not apply to parties with places of business in the U.S. unless it would also apply to the parties with places of business in the foreign states when parties with place of business in the U.S. are contracting with parties with places of business in the foreign states. See *id.*

<sup>56</sup> See, e.g., RICHARD FENTIMAN, FOREIGN LAW IN ENGLISH COURTS: PLEADING, PROOF, AND CHOICE OF LAW 29–30 (1998); OTTO KAHN-FREUND, GENERAL PROBLEMS OF PRIVATE INTERNATIONAL LAW 467 (1976); PETER MACHIN NORTH, ESSAYS IN PRIVATE INTERNATIONAL LAW 69 (1993); JUHA RATIO, THE PRINCIPLE OF LEGAL CERTAINTY IN EC LAW 114 (Francisco Laporta ed. 2003).

*Caterpillar* not only impedes the development of international sales law, it also potentially confounds Illinois state law. As the court notes, Illinois has a privity requirement for both breach of express warranty claims and breach of implied warranty claims seeking economic damages under the UCC.<sup>57</sup> *Caterpillar* was in fact barred from making any UCC claims whatsoever. The court nonetheless held that *Caterpillar* should be allowed to assert a claim under Illinois law using the doctrine of promissory estoppel. Privity of contract is obviously not required for a promissory estoppel claim in Illinois or elsewhere, but the court's decision to allow the claim raises questions about the meaningfulness of the privity requirement for UCC warranty claims. Did the court allow *Caterpillar* to do an end run around the Illinois privity requirement using the doctrine of promissory estoppel?

Under the circumstances of the case, Usinor clearly made affirmations of fact and other claims directly to *Caterpillar* that *Caterpillar* apparently relied on to its detriment in contracting to supply trucks to its customers. These circumstances, however, are close if not equivalent to those in which a party creates an express warranty under the UCC. Under the currently enacted version of the UCC in Illinois (and all other states), a seller creates an express warranty under UCC § 2-313(1)(a) by making affirmations of fact or promises that relate to the goods and become part of the "basis of the bargain."<sup>58</sup> As UCC § 2-313(1)(a) has been applied by most courts, the buyer's reliance on the seller's affirmations is essential to whether the affirmations become part of the basis of the bargain.<sup>59</sup> Nonetheless, as the official comments point out, no particular reliance needs to be shown "in order to weave [the affirmations] into the fabric of the agreement."<sup>60</sup> Once made the affirmations are presumed to become part of the basis of the bargain unless the seller can adduce facts sufficient to take them out of the agreement.<sup>61</sup>

The court in *Caterpillar* thus allowed a promissory estoppel claim in circumstances in which the plaintiff might otherwise have made a breach of express warranty claim but for the privity requirement. As the opinion made clear, there were direct communications between Usinor and *Caterpillar* which encouraged *Caterpillar* to rely on Usinor's affirmations, and other

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<sup>57</sup> *Caterpillar*, 393 F. Supp. 2d at 677, 678.

<sup>58</sup> *Id.*

<sup>59</sup> Donald J. Smythe, *The Scope of a Bargain and the Value of a Promise*, 60 S.C. L. REV. 203, 215 (2008).

<sup>60</sup> U.C.C. § 2-313 cmt. 3 (2002).

<sup>61</sup> *Id.*

courts might limit the case to similar circumstances in which the defendant communicated to the plaintiff directly. Of course, there is no logical reason why the case should be interpreted so narrowly. A downstream third party can rely on affirmations or promises that are made in advertisements or on the labels of products every bit as much as it can on those that are made through direct communications. If other courts are persuaded by *Caterpillar* and interpret it broadly then the privity requirement for breach of express warranty claims in Illinois becomes largely moot. Illinois plaintiffs will simply assert promissory estoppel claims instead. Thus, in addition to undermining the uniformity of international sales law and good faith in international trade, *Caterpillar* also confounds Illinois law.

### *B. We Have to Get Out of this Place*

There are alternative approaches to the privity problem in international sales that are much more firmly grounded in the principles of the CISG than the decision in *Caterpillar*. The most obvious alternative would simply be for courts to construe the CISG more broadly so as to preempt downstream buyers from making any domestic law claims against remote sellers. Without more, this would restrict downstream buyers in circumstances like *Caterpillar*'s to suing their immediate sellers. Their immediate sellers, of course, might then file actions against the remote sellers. Indirectly, then the remote sellers could still be made liable for damages to downstream buyers.

Of course, one problem with this alternative is that the downstream buyer might not always have a cause of action against its immediate seller. The remote seller would then evade all liabilities. And even if the downstream buyer did have a cause of action against its immediate seller it is possible that the immediate seller might not have a cause of action against the remote seller. This would allow the downstream buyer damages but it would also allow the remote seller to evade any liabilities.

Nonetheless, even if downstream buyers had no recourse this would not necessarily leave them completely vulnerable to being misled by remote sellers. If downstream buyers were precluded from filing actions against remote sellers they would probably be more likely to request that their immediate sellers reiterate any affirmations or promises made by the remote seller. This would then ensure that they had a cause of action against someone. If their immediate sellers were unwilling to reiterate the affirmations or promises then the downstream buyers would probably choose not to rely on the affirmations. Of course, this presumes that the

downstream buyers in these circumstances would have a sufficient understanding of the legal rules and enough rationality to avoid mistakenly relying on the remote sellers' promises. However, since the CISG only applies to contracts for the sale of non-household goods, it will typically only apply to parties that arguably should have at least some modicum of business sophistication.<sup>62</sup>

The great advantage of this approach is that it would achieve uniformity in the application of the CISG and promote good faith in international trade. Whether a third party had a cause of action to remedy a defect in a product would only depend on the application of the CISG, not on any Contracting State's domestic law. Courts would not be able to construe the preemptive effect of the CISG narrowly so as to apply their domestic laws to the advantage of either party. Of course, they might still exhibit a homeward trend in their application of the CISG, but this is a more general problem with international law and it is doubtful that it would create as many problems as *Caterpillar*.<sup>63</sup> In theory at least, courts should construe the CISG taking into account decisions of courts in other Contracting States.<sup>64</sup> If they follow this mandate then any homeward trend in the application of the CISG should get resolved through further developments in the case law.

Unfortunately, this approach to the problem might affect the decisions that remote sellers make about their distribution chains. For example, assume that the domestic law in Contracting State C would allow an action by a downstream buyer, Gamma, directly against a remote seller, Alpha, in Contracting State A. Under such an approach, a remote seller like Alpha would have an incentive to distribute goods in State C through an intermediary in another Contracting State – say State B – rather than directly to buyers in State C itself or through an intermediary in State C. Of course, if Alpha sold the goods directly to buyers in State C those buyers would not be downstream and they could file actions against Gamma under the CISG. Likewise, if Alpha sold the goods through an intermediary in State C the downstream buyers might be able to file claims directly against

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<sup>62</sup> See CISG, *supra* note 1, art. 2(a) (stating that CISG does not apply to sales of goods bought for personal, family or household use, unless the seller, at any time before or at the conclusion of the contract, neither knew nor ought to have known that the goods were bought for any such use).

<sup>63</sup> See the discussion *supra* note 39.

<sup>64</sup> This approach to construing the CISG would be in accordance with the direction in Article 7(1)(a) to interpret the CISG to promote uniformity in its application and good faith in international trade.

Alpha under the domestic laws of State C. On the other hand, if Alpha sold the goods to buyers in State C through an intermediary in Contracting State B – say Beta – then the CISG would apply to the contract between Beta and Gamma and this would preclude Gamma from filing claims directly against Alpha.

Of course, Alpha might still be liable to Gamma indirectly. If Gamma sued Beta under the CISG for a breach of a warranty that Beta had made based on warranties that Alpha had made to Beta, then Beta could sue Alpha under the CISG for any consequential damages.<sup>65</sup>

However, even if Alpha could be held accountable in such a manner this approach would hardly promote judicial economy. If Gamma was able to file an action directly against Alpha then there would only be a need for one lawsuit instead of two. Of course, Beta might be named as a defendant in that suit as well as Alpha, but even so Beta would only have to defend itself against one suit rather than defend itself in one suit and prosecute a second suit for consequential damages. In this respect, Beta's expected legal costs would generally be greater and it would probably pass those costs on to Alpha. It is unlikely, however, that these costs would be so high as to make some other distributional arrangement more profitable for Alpha.<sup>66</sup> From a social perspective, however, the extra legal costs incurred as a result of the indirect liability of a remote seller to a downstream buyer would be inefficient nonetheless. Moreover, these costs would likely be incurred through similar distributional arrangements in the international sale of many other goods as well. The total social costs could be quite significant.

Perhaps the greatest deficiency in this solution to the problem, however, is that it acquiesces to the privity requirement. The privity requirement is a vestige of an outmoded, narrowly doctrinal conception of

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<sup>65</sup> The CISG's damages provisions are quite liberal and allow claims for what would be considered consequential damages under the UCC. *See* CISG, *supra* note 1, art. 74 ("Damages for a breach of contract by one party consist of a sum equal to the loss, including loss of profit, suffered by the other party as a consequence of the breach.").

<sup>66</sup> If the costs were so high as to make some other distributional arrangement more profitable, of course, the point would be moot. It is highly unlikely, however, that the expected legal costs would be so great as to outweigh the benefits of distributing through an international intermediary in every case. Thus, some unnecessary social costs would almost inevitably be incurred.

contracts.<sup>67</sup> It is essentially a mechanism for ensuring that any plaintiff that proceeds with an action in contract was indeed a party to a bargain with the defendant.<sup>68</sup> Even in the late nineteenth and early twentieth century context in which the bargain theory of contract achieved ascendancy, however, the privity requirement made little sense.<sup>69</sup> The cases in which it applied then, as now, were inevitably ones similar to *Caterpillar* in which a remote seller sold goods to an intermediary who then resold them to a downstream buyer. The downstream buyer was, of course, only a third party to the contract between the remote seller and its distributor. With no privity of contract, the downstream buyer was initially precluded from bringing any actions in contract against the remote seller for damages caused by defects in the product.<sup>70</sup> Many of the suits, of course, were for damages arising from personal injuries caused by the defects.<sup>71</sup> Modern products liability law evolved out of these cases and the privity requirement was eliminated for actions in tort.<sup>72</sup> But some of the suits involved plaintiffs seeking only economic damages for defects in the product. These cases remained a matter for contracts and it is here that the privity requirement continues to play a confounding role, at least in the U.S. and other common law countries.<sup>73</sup>

The problem is not with the privity requirement itself, so much as the way in which it applies. Privity has typically been applied by courts in circumstances in which the court determined there were insufficient contacts between the parties to create contractual obligations.<sup>74</sup> Modern

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<sup>67</sup> See Smythe, *supra* note 59 (discussing the trend of courts increasingly looking to the doctrines of promissory estoppel and quasi-contract to enforce seller's promises on express warranty grounds without consideration and increasingly rejecting privity defenses).

<sup>68</sup> *Id.*

<sup>69</sup> *Id.*

<sup>70</sup> See, e.g., *Winterbottom v. Wright*, (1842) 152 Eng. Rep. 402 (Exch. Of Pleas).

<sup>71</sup> *Id.*

<sup>72</sup> See, e.g., *MacPherson v. Buick Motor Co.*, 111 N.E. 1050 (N.Y. 1916).

<sup>73</sup> As Gillette and Walt observe, "Where economic loss alone is involved, courts have been more restrictive. Where economic loss affects the value of the product itself . . . courts tend to permit actions against a distant seller. Where the economic loss is essentially consequential . . . courts have been more divided, with several continuing to require privity before permitting recovery from distant sellers." CLAYTON GILLETTE & STEVEN WALT, *SALES LAW: DOMESTIC AND INTERNATIONAL* 308 (2d ed. 2002).

<sup>74</sup> The concept of privity is slippery. Black's Law Dictionary defines privity of contract as "[t]hat connection or relationship which exists between two or more contracting parties." BLACK'S LAW DICTIONARY 1199 (6th ed. 1990). In practice, privity of contract exists wherever courts say it exists. See, e.g., *Sjajna v. General Motors Corp.*, 503 N.E.2d 760, 769 (Ill. 1986) (finding that for practical purposes privity is established when the manufacturer provides a written warranty under the Magnuson-Moss Warranty Act).

contract law revolves, of course, around the doctrine of consideration and the theory that a contract requires a bargain.<sup>75</sup> A promise does not create a contractual obligation unless it is truly bargained for.<sup>76</sup> In applying the privity requirement, therefore, courts have impliedly helped to define the scope of a bargain as it is construed under modern contract law. It makes perfect sense for courts to define and delimit the scope of a bargain. It would be absurd, for instance, for courts to allow parties to make contract claims against complete strangers. Modern tort law has developed causes of actions for parties to make against complete strangers for a variety of general legal wrongs. Indeed, the ultimate rationale for allowing tort actions is that parties cannot reasonably be expected to coordinate all of their interdependent behaviors by agreement and thus reduce all private legal actions to ones in property and contract.<sup>77</sup>

The problem with the privity requirement is not that it restricts standing to bring actions in contract to parties involved in a bargain but that the conception of a bargain under the privity requirement has been unduly narrow. In modern commercial contexts manufacturers commonly distribute goods for the mass market through a variety of intermediaries. They also commonly advertise to promote their sales and they may thus make many affirmations and promises about the quality and characteristics of their products that the ultimate buyers will see, read, or hear even though they buy the goods from intermediaries.<sup>78</sup> The manufacturers may also make affirmations or promises about their goods on the packaging in which the goods are sold or on labels on the goods themselves or perhaps even in writings sold with the goods.<sup>79</sup> American courts have struggled with the question of whether affirmations of fact or promises made in these ways create express warranties to the end consumers.<sup>80</sup> Many courts have held

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<sup>75</sup> See generally Roy Kreitner, *Calculating Promises: The Emergence of Modern American Contract Doctrine* 15–22 (2007).

<sup>76</sup> The doctrine of consideration is thus inextricably connected with the bargain theory of contracts. *Id.* at 22.

<sup>77</sup> This is one of the most interesting implications of the Coase Theorem, as elaborated by Calabresi and Melamed. Guido Calabresi & A. Douglas Melamed, *Property Rules, Liability Rules and Inalienability: One View of the Cathedral*, 85 HARV. L. REV. 1089 (1972). In a world of zero transactions costs all parties would negotiate over all interdependent behaviors in advance. See *id.* at 1094–95. There would be no need for torts because every possible private legal wrong would be covered by contract. See *id.* Of course, in the real world where transaction costs preclude such extensive contracting, tort actions are necessary to regulate many interdependent behaviors. See *id.* at 1108–09.

<sup>78</sup> See generally Smythe, *supra* note 59, at 217–24.

<sup>79</sup> *Id.*

<sup>80</sup> *Id.*

that they do, although a majority may require that the buyers actually do see, read, or hear the communications for the affirmations or promises to become part of the basis of the bargain.<sup>81</sup> In states where privity is required for a breach of an express warranty claim, of course, the question is moot. If the law requires privity for a breach of express warranty claim, and courts hold that privity cannot be established between a downstream buyer and a remote seller, then it cannot matter whether the buyer relied on the remote seller's promises. The privity requirement has barred contract claims by effectively restricting the scope of enforceable contractual bargains even when the downstream buyer did clearly rely on the remote seller's promises.

The problem, of course, is that even manufacturers that distribute goods through intermediaries are ultimately targeting downstream buyers. The use of intermediaries may help to insulate manufacturers from contract claims, but intermediaries are rarely, if ever, significant end users of the manufacturers' goods. Indeed, the reason manufacturers engage in advertising and place product information on packaging and labels is because they want to promote sales to the end buyers. It may have made sense to confine the scope of a bargain and standing to make contract claims to buyers and their immediate sellers prior to the transportation revolution in the nineteenth century that initiated the rise of mass-scale production by making the distribution of goods across vast distances and legal jurisdictions profitable,<sup>82</sup> and it may even have made sense immediately after the transportation revolution simply for reasons of judicial economy and expedience,<sup>83</sup> but it hardly makes sense in the modern era of cheap transportation and electronic communications.<sup>84</sup> If the manufacturers of mass-produced goods advertise or promote them through their packaging or labels then they can and should be considered to have contracted with anyone who might reasonably rely on the affirmations or promises contained therein.<sup>85</sup>

As a general matter, both economic efficiency and social ethics are best served by holding sellers to strict legal obligations for any affirmations

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<sup>81</sup> *Id.*

<sup>82</sup> See generally Alfred D. Chandler, Jr., *The Visible Hand: The Managerial Revolution in American Business* (1977) (providing a historical overview of commercial production and distribution in the U.S.).

<sup>83</sup> *Id.*

<sup>84</sup> GILLETTE & WALT, *supra* note 73, at 308.

<sup>85</sup> *Id.*



or promises they make about their goods.<sup>86</sup> To the extent that sellers are able to use the privity requirement to evade those obligations, the requirement only undermines economic efficiency and impedes the development of sound business ethics.<sup>87</sup> It is perhaps not surprising, therefore, that the modern trend in both American and foreign law has been towards the elimination or diminishment of the privity requirement.<sup>88</sup> The argument that the privity requirement is an obsolete vestige of the pre-modern world that undermines economic efficiency and sound business ethics has no less force in international sales law than in the domestic laws of nation states.

*C. There is a Way to Get from Here to There: The Article 16(2)(b) Approach*

The difficult question, perhaps, is can the privity requirement be eliminated from international sales transactions without undermining the integrity of the CISG? The short answer to the question is, “yes.” The wording of Article 4 limits the scope of the treaty to the rights and obligations of the seller and buyer, but the CISG does not define the term “seller” or “buyer” and the only way it offers of inferring the definition of a contract is from the provisions in Articles 12 through 23 on the formation of a contract. Given the invitation to courts to fill in the gaps in the CISG by reference to its underlying principles and to interpret its provisions in a manner that promotes good faith in international trade, this leaves open the possibility that such terms could be construed quite broadly. In fact, there are at least two possible approaches to resolving the privity problem under the CISG. One approach is to define the scope of a seller’s obligations under Article 4 broadly enough to bind a remote seller to obligations for any promises made to downstream buyers. Another approach is to interpret Article 16(2)(b) to encompass the doctrine of promissory estoppel -- or

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<sup>86</sup> Smythe, *supra* note 59, at 208–12, argues that sellers make promises in order to distinguish the quality of their products from others on the market and thus avoid the so-called “lemons problem.” Relieving sellers from liabilities for their promises only undermines their efforts, reduces the information available to buyers, and diminishes the economic efficiency of markets.

<sup>87</sup> See, e.g., CHARLES FRIED, *CONTRACT AS PROMISE: A THEORY OF CONTRACTUAL OBLIGATIONS* 19 (1981) (articulating a moral obligation to keep promises regardless of whether consideration is present).

<sup>88</sup> See JOHN O. HONNOLD & CURTIS R. REITZ, *SALES TRANSACTIONS: DOMESTIC AND INTERNATIONAL LAW* 272, 291–92 (3d ed. 2006); JOHN O. HONNOLD, *UNIFORM LAW OF INTERNATIONAL SALES* § 63 (3d ed. 1999); JAMES J. WHITE & ROBERT S. SUMMERS, *UNIFORM COMMERCIAL CODE* § 11-7 (5th ed. 2002).

something very much like it. Both of these approaches would arguably be consistent with the CISG's underlying principles.

One distinguished commentator, John Honnold, has argued that Article 4 may be interpreted to extend the obligations of a remote seller under the CISG to encompass promises or guarantees that it makes to downstream buyers.<sup>89</sup> On this view, the promises or guarantees made by the remote seller to the downstream buyer are a part of a larger commercial contract in which the downstream buyer's immediate seller is merely an intermediary.<sup>90</sup> Technically, the remote seller need not be construed as the downstream buyer's "seller" but the transaction between the remote seller and downstream buyer can still be construed as a "contract of sale."<sup>91</sup> This approach is more compelling the more the remote seller does to encourage the downstream buyer to make the purchase. Promises or guarantees made by the remote seller itself are more likely to create a unilateral contract than promises or guarantees that are impliedly made by the remote seller through its controls over an intermediary dealer under the terms of a franchise agreement.<sup>92</sup> As Honnold cautions, however, if the downstream buyer and the remote seller's dealer have places of business in the same Contracting State the CISG would not apply to the contract.<sup>93</sup>

One potential problem with this approach is that it might logically imply that the remote seller is also liable for other claims under Article 35 – claims that resemble implied warranties in U.S. law. If the remote seller's

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<sup>89</sup> HONNOLD, *supra* note 43, at 76. Honnold acknowledges that this is a change in position on the issue from the one he had taken in earlier editions of the book, in which he had opined that the language of Article 4 limited the seller's obligations to the immediate buyer. *Id.* Honnold, in fact, observes that the court in *Asante*, 164 F. Supp. 2d 1142 (N.D. Cal. 2001), did allow a U.S. buyer to make claims against a remote Canadian manufacturer, although the court appeared to be "blithely unaware of any issues raised by the fact that the claim was against a party who had not sold the goods directly to the buyer." *Id.* at 78. Honnold nonetheless concludes that "it is unlikely that the Convention in the foreseeable future will play a large role in claims by buyers against manufacturers and similar remote suppliers." *Id.* at 77.

<sup>90</sup> *Id.* at 76.

<sup>91</sup> *Id.* at 77.

<sup>92</sup> *Id.*

<sup>93</sup> *Id.* at 77. Of course, in the case where the downstream buyer and the remote seller's dealer have places of business in the same Contracting State the contract between the remote buyer and the dealer would be governed by the domestic law of the buyer's and dealer's locations. In the U.S. this would mean some state's version of Article 2 of the UCC would be the applicable law. In many states privity is not required for an express warranty claim and so the manufacturer might well be liable under domestic law. GILLETTE & WALT, *supra* note 73, at 308.

promises or statements are construed to make the larger transaction between the remote seller and downstream buyer a contract of sale under the CISG then all the other provisions of the CISG would arguably apply, including the implied warranty-like provisions in Article 35.<sup>94</sup> This could be problematic. Article 35 expressly authorizes the parties to contract around these implied warranty-like provisions.<sup>95</sup> The CISG arguably also authorizes the parties to contract around the damages provisions, including the provision in Article 74 for consequential damages.<sup>96</sup> Sophisticated sellers often do seek to limit or exclude their exposure to implied warranties and consequential damages. It is difficult to imagine how a remote seller in a foreign Contracting State could limit or exclude implied warranties and consequential damages in a contract of sale that is implied rather than bargained-for with a downstream buyer.

Articles 14(2) and 16(2)(b) of the CISG offer an alternative approach to the privity problem that may therefore be even more appealing and might also prove to be more flexible in application. Article 14(2) provides that offers may be made to indefinite persons;<sup>97</sup> Article 16(2)(b) states a provision that to those trained in the common law seems redolent of the doctrine of promissory estoppel, even though it is not stated in those

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[T]he goods do not conform with the contract unless they: (a) are fit for the purposes for which goods of the same description would ordinarily be used; (b) are fit for any particular purpose expressly or impliedly made known to the seller at the time of the conclusion of the contract, except where the circumstances show that the buyer did not rely, or that it was unreasonable for him to rely, on the seller's skill and judgment.

CISG, *supra* note 1, art. 35(2)(a).

<sup>95</sup> *See id.* art. 35(2). Article 35(2) begins with the qualification, "Except where the parties have agreed otherwise . . ." Thus, it reiterates that the parties may exercise the autonomy to contract around the implied-warranty-like provisions otherwise granted more generally in Article 6. Article 6 states: "The parties may exclude the application of this Convention or, subject to Article 12, derogate or vary the effect of any of its provisions."

<sup>96</sup> *Id.* art. 74 ("Damages for breach of contract consist of a sum equal to the loss, including loss of profit, suffered as a consequence of the breach."). Article 6 presumably implies that the parties can derogate or vary the effect of this provision, including the part relating to consequential damages. *See id.* art. 6 ("The parties may exclude the application of this Convention or, subject to article 12, derogate from or vary the effect of any of its provisions.").

<sup>97</sup> *Id.* art. 14(2) ("A proposal other than one addressed to one or more specific persons is to be considered merely as an invitation to make offers, unless the contrary is clearly indicated by the person making the proposal.").

terms.<sup>98</sup> However, it is important to remember that the CISG was a compromise between representatives from diverse legal systems and the drafters had to accommodate both common and civil law traditions.<sup>99</sup> Although Corbin speculated that it would be unnecessary for civil law countries to develop a theory of enforcement based on reliance because they could simply make enforceable every promise upon which it would be reasonable to rely, in general European legal systems have not provided much protection to promisees who rely on promises.<sup>100</sup> Article 16(2)(b) in some sense may split the difference. Although it is strongly redolent of the common law doctrine of promissory estoppel it established a reliance based theory for enforcing offers without using the concept of estoppel. In principle, this means that Article 16(2)(b) could be used as a “sword” and not just a “shield” – in other words, it could be used by downstream buyers to make claims against remote sellers under circumstances like those in *Caterpillar*.<sup>101</sup>

Indeed, Henry Mather has noted the resemblances between Article 16(2)(b) and the doctrine of promissory estoppel under U.S. law.<sup>102</sup> There are, however, also some important differences: Article 16(2)(b) does not require that the offeree’s reliance must have been foreseeable to the offeror or that the offeree’s reliance be detrimental to the offeree.<sup>103</sup> Nonetheless, Mather has predicted that “many tribunals will apply [Article 16(2)(b)] in much the same fashion as American courts have used promissory

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<sup>98</sup> *Id.* art. 16(2) (“However an offer cannot be revoked: (a) if it indicates, whether by stating a fixed time for acceptance or otherwise, that it is irrevocable, or (b) if it was reasonable for the offeree to rely on the offer as being irrevocable and the offeree has acted in reliance on the offer.”). As Mather writes, “[Article 16 2(b)] looks very much like American promissory estoppel doctrines, although it does not expressly require that the offeree’s reliance must have been foreseeable to the offeror and does not expressly require that the offeree’s reliance be detrimental.” Henry Mather, *Firm Offers Under the UCC and the CISG*, 105 DICK. L. REV. 31, 48 (Fall 2000).

<sup>99</sup> Andrea Vincze, *Revocability of offer: Remarks on whether and the extent to which the UNIDROIT Principles may be used to help interpret Article 16 of the CISG*, in FELEMEGAS, *supra* note 40, at 85 (observing that CISG, Article 16(2)(a) was included to incorporate the civil law concept of irrevocable offers and CISG, Article 16(2)(b), which is very similar to the doctrine of promissory estoppel, was included to accommodate the common law).

<sup>100</sup> JAMES GORDLEY, *THE ENFORCEABILITY OF PROMISES IN EUROPEAN CONTRACT LAW* 343 (2001).

<sup>101</sup> Historically, the doctrine of promissory estoppel arose as a defense to an action brought by another rather than as a basis for a cause of action itself. *Id.* at 58, 62.

<sup>102</sup> See, e.g., Mather, *supra* note 97; Vincze, *supra* note 98.

<sup>103</sup> Mather, *supra* note 97, at 48.

estoppel.”<sup>104</sup> Indeed, the federal district court for the Southern District of New York has agreed with this interpretation of Article 16(2)(b) in *Geneva Pharmaceuticals Technology Corp v. Barr Laboratories, Inc.*<sup>105</sup> As the court explained, Article 16(2)(b) “establishes a modified version of promissory estoppel that does not appear to require foreseeability or detriment, and to apply an American . . . version of promissory estoppel.”<sup>106</sup> The court therefore concluded that domestic promissory estoppel claims could be preempted by the CISG.<sup>107</sup>

Article 16(2)(b) thus appears to provide a basis for holding remote sellers like Usinor to claims by downstream buyers like Caterpillar for any promises they make in the marketing and distribution of their goods. Hypothetically, if the court in *Caterpillar* had followed the court in *Geneva Pharmaceuticals* the same logic that it had used to apply the doctrine of promissory estoppel under Illinois law could have been applied to allow Caterpillar to make a CISG claim against Usinor under Article 16(2)(b). Apparently, however, Caterpillar neglected to state a claim against Usinor under Article 16(2)(b) and so this is only a conjecture. The facts in *Caterpillar* are, however, quite specific: Caterpillar alleged that Usinor made representations about its steel directly to Caterpillar prior to contracting with CMSA. Caterpillar also alleged that it relied on those representations to its detriment. Under those facts, the court applied promissory estoppel. It is not clear, however, whether the court would have applied promissory estoppel if Usinor had not made the representations directly to Caterpillar. What if Usinor had made the same statements of fact about its steel in advertisements or brochures or other promotional materials rather than directly to Caterpillar?

In other words, does Article 16(2)(b) provide a basis under the CISG for downstream buyers to make claims against remote sellers for statements or representations the remote sellers make about their products that would be sufficient to create warranties under Article 35 to their immediate buyers? Logic suggests it does. Indeed, since Article 16(2)(b) suggests there are no foreseeability or detriment requirements for promissory estoppel-like claims under the CISG it would appear to be sufficient for the downstream buyer to read, see, or hear the remote seller’s statements or representations about the product before purchasing the remote seller’s goods from its immediate seller for the downstream buyer to hold the remote seller liable.

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<sup>104</sup> *Id.*

<sup>105</sup> *Geneva Pharm.*, 201 F. Supp. 2d 236 at 236.

<sup>106</sup> *Id.*

<sup>107</sup> *Id.*

Article 16(2)(b) thus could provide a basis under the CISG for holding remote sellers liable for statements sufficient to create the CISG equivalent of express warranties under Article 35(1).

The question is whether courts will take up the opportunity. They should. The privity requirement for express warranty claims makes little sense in the modern commercial world where sellers place their goods in the stream of commerce with the knowledge that they will often be resold in foreign nations. Construing the CISG to require privity of contract simply protects remote sellers from liabilities for claims they make in their advertisements and promotional materials that are clearly intended to increase their sales to downstream buyers. It thus undermines the reliability and value of the information in those advertisements and promotional materials.<sup>108</sup> It may therefore undermine the incentives for sellers to provide such information altogether and thus reduce the amount of information available to buyers overall.<sup>109</sup> Since this kind of information is an antidote to the “lemons problem,” inhibiting sellers from providing it or diminishing its value to buyers is likely to cause an economic inefficiency.<sup>110</sup>

It is also likely to impede good faith in international trade. One of the bedrock propositions of Kantian moral theory is that it is wrong for a person to make a promise without intending to keep it.<sup>111</sup> It is true that the CISG is an international treaty between nation states with diverse legal systems and perhaps equally diverse mores and social values, but most cultures place great moral value on the keeping of promises and would likely adhere to this Kantian precept.<sup>112</sup> Most would probably agree, therefore, that a seller that made statements about its good in advertisements or other promotional material without intending to keep them would be acting in bad faith. Courts could thus promote good faith in international trade by holding sellers liable for the statements they make in their advertising and promotional materials, regardless of whether the sellers are in privity of contract with the buyers who make the claims. Such an approach would be faithful to the mandate in Article 7(1).

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<sup>108</sup> The argument is analogous to the one provided by Smythe against the reliance test that courts commonly apply to determine whether express warranties have been made under UCC § 2-313(1)(a). Smythe, *supra* note 59, at 216–236.

<sup>109</sup> *Id.*

<sup>110</sup> *Id.*

<sup>111</sup> See Sharon Byrd & Joachim Hruschka, *Kant on Why I Must Keep My Promise*, 81 CHI.-KENT L. REV. 47 (2006) (discussing Kant’s ethics concerning promises and the legal implications of those ethics).

<sup>112</sup> See generally P.S. Atiyah, *the Rise and Fall of Contract* 41–60 (1979).

Finally, holding remote sellers liable for the statements they make, directly or indirectly, to downstream buyers would also help to promote uniformity in the application of the CISG as also required under Article 7(1). Since some courts, such as the court in *Caterpillar*, may be tempted to allow downstream buyers to make domestic legal claims against remote sellers if the CISG is construed to preclude similar CISG claims, non-uniform domestic rules governing privity requirements may control. Indeed, these non-uniform rules could encourage not only forum-shopping but also distort the decisions that remote sellers make about their distribution systems and the locations of their distributors.<sup>113</sup> By allowing downstream buyers to make claims under the CISG instead, courts would not only promote uniformity in international sales law, they would also advance international justice and encourage economic efficiency.

### Conclusion

The CISG was intended to facilitate and promote international trade by improving the governance and legal certainty of international sales contracts. Unfortunately, it offers a set of rules that are rather sparse in comparison with those of the UCC and presumably also the domestic laws of other Contracting States. This invites parties to a CISG dispute to claim that important questions fall within its gaps and thus argue for the application of a favorable domestic legal rule to fill the gap. Courts have frequently accepted these claims and thus applied domestic rules in disputes under the CISG. This obviously confounds the purpose of the CISG and will only impede the expansion of international trade and commerce. One important matter that courts will inevitably have to address is whether downstream buyers can make any CISG claims against remote sellers, and, if not, whether they can then make any domestic legal claims.

The manner in which the U.S. federal district court for the Northern District of Illinois addressed the issue in *Caterpillar v. Usinor* illustrates the magnitude of the problem. The court in *Caterpillar* limited the preemptive effect of the CISG to domestic contract claims by the remote seller's immediate buyer. The court held the downstream buyer could make any domestic contract claims against the remote seller that would be viable under state law. Illinois has privity requirements for UCC breach of warranty claims so these were not viable. The court nonetheless allowed the downstream buyer to make a promissory estoppel claim under Illinois

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<sup>113</sup> See *supra* discussion in Part II.A.

common law. The case thus not only confounds the purpose of the CISG, it also confounds Illinois state law. It provides yet another example of the homeward trend bias that threatens to undermine efforts to unify international commercial law.

The best antidote to the problem is to encourage courts to construe the preemptive effect of the CISG broadly to define all the rights and obligations of the seller and buyer. Of course, this creates another dilemma: because the CISG's rules are sparse courts will either have to define the rights and obligations of the seller and buyer very narrowly or find expansive ways of construing the CISG's terms and principles. Claims by downstream buyers against remote sellers are a case in point. If Article 4 of the CISG is defined narrowly, so as to require privity for CISG claims, then international sales law will remain underdeveloped and ill-suited to address contracting problems in the modern commercial world. It is possible, however, to define Article 4 more broadly and to find ways of allowing downstream buyers to make claims against remote sellers for any statements or promises the remote sellers make about their goods that would be sufficient to create obligations to their immediate buyers under Article 35.

One possibility is to construe the downstream buyer and remote seller as parties to a contract of sale. This approach could be problematic since it might also make remote sellers liable for other obligations to their downstream buyers under the CISG -- obligations that they might choose to limit or modify if they were actually able to bargain. There is, however, a better alternative. Article 16(2)(b) has been construed by both commentators and courts to resemble the common law doctrine of promissory estoppel. In principle, therefore, courts should be able to construe Article 16(2)(b) to allow downstream buyers to make claims against remote sellers in exactly the same circumstances as those that presented themselves in *Caterpillar v. Usinor*. In fact, this essay has argued that Article 16(2)(b) can be construed to allow downstream buyers to make claims against remote seller for any statements or promises the remote sellers have made in advertisements or other promotional materials whenever the downstream buyers purchased the goods after seeing, reading, or hearing them. The irony is that some reflection upon the court's holding in *Caterpillar* suggests a solution to a much larger problem: how to eliminate the privity requirement from international sales transactions without undermining the integrity of the CISG.



## The New York Appeal: An Analysis of the Forum Non Conveniens Doctrine in U.S. Letter of Credit Litigation

Eric C. Williams\*

### Introduction

The modern transaction is not your father's transaction. Today, transactions are increasingly international.<sup>1</sup> Consider this common scenario: John, a widget maker in Macau, contracts with Jane, a factory owner in Omaha, for the sale of widgets. However, John wants insurance that he will receive payment, so he requests the credit of a New York bank, ABC, as an independent guarantee of payment.<sup>2</sup> If Jane still wants to purchase John's widgets, she will have to obtain issuance of a letter of credit by ABC. ABC pays John once he presents conforming documentation specified in the letter of credit,<sup>3</sup> including evidence of shipment of the widgets to Jane. ABC then seeks reimbursement from Jane, who takes the conforming documentation and retrieves her widgets.<sup>4</sup>

However, suppose that John presented documentation specified in the letter of credit, but ABC was dissatisfied with the presentation and refused to honor the credit.<sup>5</sup> John sues ABC for wrongful dishonor, but in

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<sup>1</sup> See Kimberly Hicks, Note, *Parallel Litigation In Foreign and Federal Courts: Is Forum Non Conveniens the Answer?*, 28 REV. LITIG. 659, 662 (2009) ("Parallel litigation has always been present, but it has become more prevalent over the last twenty-five years for two main reasons: more interaction across sovereign borders and more liberal personal jurisdiction rules.").

<sup>2</sup> See *infra* notes 58–66 and accompanying text.

<sup>3</sup> See *infra* note 63 and accompanying text.

<sup>4</sup> See *infra* notes 65–66 and accompanying text.

<sup>5</sup> Common reasons why an Issuer would be dissatisfied with a Beneficiary include fraud, late or inadequate notice, or non-compliance of the terms and conditions of the letter of credit. See, e.g., *Banco General Runinahui, S.A. v. Citibank Int'l*, 97 F.3d 480, 483 (11th Cir. 1996) (Issuer refused to honor Beneficiary's request because the documents submitted contained several discrepancies); *Avery Dennison Corp. v. The Home Trust & Savs. Bank*, 2003 WL 22697175, at \*2 (N.D. Iowa Nov. 7, 2003) (Issuer refused to honor Beneficiary's demand because it fell outside the deadline, which stated that 3:00 PM on Fridays was Monday business); *Amwest Sur. Ins. Co. v. Concord Bank*, 248 F. Supp. 2d 867, 872 (E.D. Mo. 2003) (Issuer dishonored Beneficiary's draft because, allegedly, it violated a letter of credit condition that stated Beneficiary would not be released of liability by its obligees).

which forum should he file his action? At least three come to mind—Macau, a federal district court in New York, or a federal district court in Nebraska. Alternatively, suppose that Jane sued ABC for wrongful honor of the letter of credit. Where should she file her claim? Moreover, assuming in either suit that ABC moved to dismiss on forum non conveniens grounds, would a court likely grant or deny the motion?

Because letter of credit transactions stretch parties across continents, its litigation generates a steady flow of actions that turn on the doctrine of forum non conveniens. This Comment will survey how U.S. courts interpret the doctrine in letter of credit litigation. Case law reveals two attitudes that courts have embraced, in whole or in part, when they are confronted by this type of litigation: (1) for denying (or dismissing) the application of forum non conveniens, because the court's forum, and thus its financial market, has superseding interest in the letter of credit litigation;<sup>6</sup> or (2) for granting (or upholding) the application of forum non conveniens, because the limited contacts presented by plaintiff would otherwise open a flood gate and turn the forum into a melting pot for complex foreign issues.<sup>7</sup>

Both attitudes are legitimate and important, especially considering that the United States, particularly New York, is home to substantial sums of international letter of credit business.<sup>8</sup> This Comment will first provide the necessary background for understanding forum non conveniens and letters of credit. It will also delve into the governing framework of letter of credit transactions for choices of law and forum; that is, the UCP and revised U.C.C. Article 5. The Comment will then begin analyzing, what it calls, the 'New York' effect. The financial backdrop of a forum, at least in part, can induce courts to protect litigation from being heard in alternate forums. No contact is more substantial than the market itself and, therefore, no other forum has greater interest to hear litigation born out of, and affecting, that market.<sup>9</sup> The Comment will counter this analysis with, what it also calls, the 'melting pot' effect. When facts primarily occurred in a

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<sup>6</sup> See, e.g., *J. Zeevi & Sons, Ltd. v. Grindlays Bank (Uganda) Ltd.*, 37 N.Y.2d 220, 227 (1975) ("New York has an overriding and paramount interest in the outcome of this litigation."); *Intercontinental Planning, Ltd. v. Daystrom, Inc.*, 24 N.Y.2d 372, 383–84 (1969) ("The Legislature intended to protect not only its own residents but also those who come into New York and take advantage of its position as an international clearing house and market place.").

<sup>7</sup> See *infra* note 126 and accompanying text.

<sup>8</sup> See *First Union Nat'l Bank v. Paribas*, 135 F. Supp. 2d 443, 453 (S.D.N.Y. 2001) ("This Court is quite mindful [of New York] as a world financial capital . . .").

<sup>9</sup> See *infra* note 78 and accompanying text.

foreign country by mostly foreign participants, but the plaintiff is belaboring minimal U.S. contacts, while the defendant is pointing to foreign law or, better yet, to a foreign forum, a cluster of complex issues begins melting before the court. It is the court's job to wade through the relative interests melting in the pot and determine *which* contact is the most substantial and *where* it is the most substantial. This comparison is untapped in the letter of credit community and will yield beneficial analysis for practitioners and scholars alike.

## I. Background

Background commentary proceeds in two sections. The first section highlights matters that are relevant to understanding forum non conveniens for purposes here. The section introduces the procedural effects of the *Gulf Oil*<sup>10</sup> and *Piper*<sup>11</sup> decisions, particularly how each continues to force its impression on current interpretation of procedural law. Special attention is also devoted to actions involving foreign plaintiffs, as these are common in letter of credit litigation. Finally, the section overviews scholarly interpretation of the public and private interests attached to reviewing a motion for forum non conveniens.

The second background section discusses the fundamentals of a letter of credit transaction. By their nature, letters of credit draw together foreign parties and transnational dealings. This is why a letter of credit and the doctrine of forum non conveniens, incongruous as they are, actually draw relevant connections. The section breaks down the parties and multiple contracts that are associated with a letter of credit transaction. Finally, the section discusses the standard governing frameworks of a letter of credit—the UCP and the U.C.C.

### A. Forum Non Conveniens

Forum non conveniens is an important doctrine of American procedural law. Under 28 U.S.C. § 1404(a), Congress authorized that, “[f]or the convenience of parties and witnesses, in the interest of justice, a district court may transfer any civil action to any other district or division where it might have been brought.”<sup>12</sup> This doctrine holds that a forum, although appropriate under the law, may divest itself from hearing an action if, out of convenience for litigants and witnesses, the action proceeded in an alternate

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<sup>10</sup> *Gulf Oil Corp. v. Gilbert*, 330 U.S. 501 (1947).

<sup>11</sup> *Piper Aircraft Co. v. Reyno*, 454 U.S. 235 (1981).

<sup>12</sup> 28 U.S.C. § 1404(a) (1996).

forum where it could—or, perhaps, *should*—have originally been brought.<sup>13</sup> In federal court, however, § 1404(a) applies only when the alternate forum is within the United States.<sup>14</sup> In this respect, § 1404(a) is a “statutory substitute”<sup>15</sup> for the common law expression *forum non conveniens*. The doctrine truly applies in federal court only when the alternate forum is in a foreign territory.<sup>16</sup>

Today, when deciding a *forum non conveniens* motion, courts primarily assess three criteria: (1) availability of an alternate forum; (2) degree of deference to plaintiff’s chosen forum; and (3) where public and private interests will best be served.<sup>17</sup> In *Gulf Oil Corp. v. Gilbert*,<sup>18</sup> the U.S. Supreme Court materialized the doctrine of *forum non conveniens* when it held that courts should defer to plaintiff’s private choice of forum unless this deference grossly disadvantaged the defendant, such as imposing excessive expenses on his defense.<sup>19</sup> In assessing the impact on private interests, a court was to weigh the parties’ accessibility to evidence; the availability of willing and unwilling witnesses, as well as the cost and convenience associated with each one attending trial; and the enforceability of a final judgment.<sup>20</sup> Additionally, the Court held for the consideration of public interests when applying *forum non conveniens*.<sup>21</sup> One interest was the backlog of the chosen forum’s case docket, regardless of whether the action originated in the chosen forum.<sup>22</sup> A second interest was that, if plaintiff requested a jury trial, the Court discouraged citizens from hearing and ruling on an action that did not affect their community, especially if their ruling impinged upon another community.<sup>23</sup>

The Court expanded on this latter consideration in *Piper Aircraft Co. v. Reyno*.<sup>24</sup> Plaintiff represented the estates of Scottish citizens, who were killed in an airplane crash over Scotland.<sup>25</sup> Plaintiff brought wrongful

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<sup>13</sup> BLACK’S LAW DICTIONARY 544 (8th ed. 2005).

<sup>14</sup> *Ravelo Monegro v. Rosa*, 211 F.3d 509, 512–13 (9th Cir. 2000) (explaining that § 1404(a) “serves as a statutory substitute for *forum non conveniens* in federal court when the alternative forum is within the territory of the United States.”).

<sup>15</sup> *Id.*

<sup>16</sup> *Id.* at 513.

<sup>17</sup> John Fellas, *Choice of Forum in International Litigation*, 721 PLI/LIT 261, 291 (2005).

<sup>18</sup> 330 U.S. 501 (1947).

<sup>19</sup> *Id.* at 508.

<sup>20</sup> *Id.*

<sup>21</sup> *Id.*

<sup>22</sup> *Id.*

<sup>23</sup> *Id.* at 508–09.

<sup>24</sup> 454 U.S. 235, 260 (1981).

<sup>25</sup> *Id.* at 238.

death actions against defendant-plane manufacturer,<sup>26</sup> which were combined and transferred to federal district court in Pennsylvania.<sup>27</sup> Defendant quickly moved to dismiss given that an alternative forum existed in Scotland.<sup>28</sup> The district court granted dismissal, but the Third Circuit reversed, in part on grounds that *forum non conveniens* should not ““result in a change in the applicable law.””<sup>29</sup> *Forum non conveniens* was justifiable only if American law was inapplicable, or if the foreign jurisdiction, by its own choice of law, gave plaintiff “the [same] benefit of the claim to which she [was] entitled . . . .”<sup>30</sup> The Supreme Court disagreed and reversed.<sup>31</sup>

The Supreme Court held that if *forum non conveniens* (a) changed applicable law and (b) disadvantaged plaintiff, these, by themselves, were insufficient to prevent dismissal.<sup>32</sup> Had the Court held differently, trial courts would have to perform “complex exercises in comparative law.”<sup>33</sup> The exercises would include a determination of what law applied to the plaintiff’s chosen forum and to the alternate forum and, if different, a comparison of the rights, remedies, and procedures available under each applicable law.<sup>34</sup> A dismissal based on *forum non conveniens* would be appropriate only if the alternate forum afforded plaintiff as much favor as his chosen forum.<sup>35</sup> Having these exercises would burden trial courts and render *forum non conveniens* “virtually useless.”<sup>36</sup>

The superseding point to draw from *Gilbert* and *Piper* is that *forum non conveniens* was partly designed to save courts the burden and expense

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<sup>26</sup> *Id.*

<sup>27</sup> *Id.*

<sup>28</sup> *Id.*

<sup>29</sup> *Reyno v. Piper Aircraft Co.*, 630 F.2d 149, 164 (3d Cir. 1980) (holding that “a dismissal for *forum non conveniens*, like a statutory transfer, ‘should not, despite its convenience, result in a change in the applicable law.’” (quoting *DeMateos v. Texaco, Inc.*, 562 F.2d 895, 899 (3d Cir. 1977))), *rev’d*, 454 U.S. 235 (1981).

<sup>30</sup> *Id.*

<sup>31</sup> *Piper*, 454 U.S. at 238.

<sup>32</sup> *Id.* (“[T]he possibility of an unfavorable change in law should not, by itself, bar dismissal . . . .”).

<sup>33</sup> *Id.* at 251.

<sup>34</sup> *Id.*

<sup>35</sup> *Id.*

<sup>36</sup> *Id.* at 250 (The Court explained that since requirements for jurisdiction and venue are easy for plaintiffs to satisfy, plaintiffs can typically choose from several legitimate forums, but will be inclined to select the forum “whose choice-of-law rules are most advantageous.” Therefore, “if the possibility of an unfavorable change in substantive law is given substantial weight in the *forum non conveniens* inquiry, dismissal would rarely be proper.”).

of comparative exercises<sup>37</sup> and, instead, to have them rely more on discretion. Public interest concerns suggest dismissal when a court is “required to ‘untangle problems in conflict of laws, and in law foreign to itself.’”<sup>38</sup> However, this complexity captures the essence of today’s forum non conveniens motion. A foreign plaintiff, who is looking to file his action in a plaintiff-friendly American court, will do so in a forum that is convenient for defendant because, most likely, it is defendant’s home forum.<sup>39</sup> The *Piper* court held that a foreign plaintiff’s choice of forum “deserves less deference.”<sup>40</sup> The Ninth Circuit, however, clarified that “less deference is not the same thing as no deference.”<sup>41</sup> The clarification points toward the “conventional wisdom”<sup>42</sup> that choice-of-law doctrine does not substantially influence a court’s choice-of-law decisions.<sup>43</sup> The decisions, instead, are more likely motivated by biases that favor American law before foreign law,<sup>44</sup> American “over foreign litigants, and plaintiffs over defendants.”<sup>45</sup> These biases, however, do not diminish the one constant of the forum non conveniens doctrine: that no case today, which involves foreign parties in a transnational dispute, “is immune from the forum non conveniens battle.”<sup>46</sup>

Since *Piper*, scholars have argued that public and private interests should be less of a balancing test and more of a hierarchical checklist, where public interests are considered only after private interests favor

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<sup>37</sup> *Id.* at 251 (construing that “[t]he doctrine of *forum non conveniens* . . . is designed in part to help courts avoid conducting complex exercises in comparative law.”).

<sup>38</sup> *Id.* (quoting *Gulf Oil Corp. v. Gilbert*, 330 U.S. 501, 509 (1947)).

<sup>39</sup> See *Ravelo Monegro v. Rosa*, 211 F.3d 509, 513 (9th Cir. 2000) (“[F]oreign plaintiffs typically bring such suits in the quintessentially convenient forum for the defendant[—]the defendant’s home forum.”).

<sup>40</sup> *Piper*, 454 U.S. at 256.

<sup>41</sup> *Ravelo*, 211 F.3d at 514; see also Elizabeth T. Lear, *Congress, the Federal Courts, and Forum Non Conveniens: Friction on the Frontier of the Inherent Power*, 91 IOWA L. REV. 1147, 1150 (2006) (admitting that even with the Ninth Circuit’s holding, “it is not at all clear what the forum non conveniens standard is.”).

<sup>42</sup> Christopher A. Whytock, *Myth or Mess? International Choice of Law Action*, 84 N.Y.U. L. REV. 719, 721 (2009) (citing Stewart E. Stark, *The Marginal Relevance of Choice of Law Theory*, 142 U. PA. L. REV. 949, 951 (1994); Symeon C. Symeonides, *Choice of Law in the American Courts in 1994: A View “From the Trenches”*, 43 AM. J. COMP. L. 1, 2 (1995)).

<sup>43</sup> *Id.*

<sup>44</sup> *Id.* (citing Joseph William Singer, *Real Conflicts*, 69 B.U. L. REV. 1, 59 (1989); Ralph U. Whitten, *U.S. Conflict-of-Laws Doctrine and Forum Shopping, International and Domestic (Revisited)*, 37 TEX. INT’L L.J. 559, 560 (2002)).

<sup>45</sup> *Id.* (citing Lea Brilmayer, *Interest Analysis and the Myth of Legislative Intent*, 78 MICH. L. REV. 392, 398 (1980)).

<sup>46</sup> Lear, *supra* note 41, at 1150–51.

granting the motion.<sup>47</sup> Otherwise, if the motion transferred an American plaintiff's action out of an American court, he would be deprived of access to the American legal system out of respect for administrative inconvenience.<sup>48</sup> Professor Martin Davies argues that this substantial result should be carried out, not by the court's decree, but only "if it is dictated by the convenience of the parties themselves or by the complete absence of any connection between the dispute and the U.S. forum."<sup>49</sup> Emily Derr adds that *Gilbert* did not outline public interest considerations for an "international context."<sup>50</sup> Therefore, public interest factors should be reserved under an analysis of jurisdictional and venue rules, and should defer to forum non conveniens only when these rules prove insufficient.<sup>51</sup>

### B. Letter of Credit Transactions

Despite Davies' and Derr's insistence that courts should stray from interpreting the doctrine with practical, public interest underpinnings,<sup>52</sup> courts still tend to do so. This is why actions where defendants move to dismiss on forum non conveniens grounds commonly involve foreign litigants in global disputes.<sup>53</sup> To be sure, two foundational elements of many letters of credit are foreign parties and international commercial transactions. Therefore, the availability of a forum non conveniens motion can be an important factor in U.S. letter of credit litigation.

The Uniform Commercial Code (U.C.C.), which is an "integrated model law"<sup>54</sup> adopted in some version by all U.S. territories and "regarded

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<sup>47</sup> See, e.g., Emily J. Derr, Note, *Striking a Better Public-Private Balance In Forum Non Conveniens*, 93 CORNELL L. REV. 819, 822 (2008) (construing that "judges should approach the forum non conveniens analysis with the understanding that the public interest factors are merely supplementary: a court should consider the public interest factors only if a private interest factor also weighs in favor of dismissal.").

<sup>48</sup> Martin Davies, *Time to Change the Federal Forum Non Conveniens Analysis*, 77 TUL. L. REV. 309, 373 (2002); see also Derr, *supra* note 47, at 842 (construing that "[a]dministrative inconvenience is an insufficient reason to deprive American citizens of their legitimate expectation that a U.S. forum will hear their disputes that satisfy jurisdictional rules and do not inconvenience the parties.").

<sup>49</sup> Davies, *supra* note 48.

<sup>50</sup> Derr, *supra* note 47, at 842.

<sup>51</sup> *Id.* at 845.

<sup>52</sup> See *supra* notes 47–51 and accompanying text.

<sup>53</sup> See Lear, *supra* note 41, at 1150–51 (construing that "it is not at all clear what the forum non conveniens standard is. What is clear is that virtually no case involving a transnational event is immune from a forum non conveniens battle.").

<sup>54</sup> LC RULES & LAWS: CRITICAL TEXTS 137 (James E. Byrne ed., 4th ed. 2007) [hereinafter LC RULES & LAWS].

by federal courts as declaratory of federal common law,<sup>55</sup> defines a letter of credit as:

[A] definite undertaking that satisfies the requirements of [U.C.C. §] 5-104 by an issuer to a beneficiary at the request or for the account of an applicant or, in the case of a financial institution, to itself or for its own account, to honor a documentary presentation by payment or delivery of an item or value.<sup>56</sup>

A traditional letter of credit transaction involves two distinct contracts and normally three separate parties.<sup>57</sup>

First, in simplest contract terms, a buyer contracts with a seller for goods or services. This contract is the original, underlying transaction of the letter of credit.<sup>58</sup> If the seller wants assurance that he will receive payment for his goods or services, because the buyer is foreign, unproven, or unreliable, then the seller may request “the credit of a third party, usually a bank, as an independent guarantee of payment to protect the parties.”<sup>59</sup> The buyer, in contracting with this seller, in effect promises to establish a letter of credit with the third party-bank for the purchase price amount.<sup>60</sup> In this respect, the buyer is called the *Applicant*, or the “person at whose request or for whose account a letter of credit is issued.”<sup>61</sup> The third party-bank is called the *Issuer* or *Issuing bank*, because it issues the letter of credit for the buyer-applicant in favor of the seller.<sup>62</sup> In doing so, the issuing bank promises to pay the seller once he presents appropriate documentation as

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<sup>55</sup> *Id.*

<sup>56</sup> U.C.C. § 5-102(a)(10) (1995).

<sup>57</sup> *Cf.* In re Graham Square, Inc., 126 F.3d 823, 827 (6th Cir. 2004) (explaining that a letter of credit transaction comprises three distinct contracts: first, the underlying contract, between the buyer and seller; second, a so-called *contract* between the buyer-applicant and the third party-bank issuing the letter of credit; and third, the letter of credit issued by the bank in favor of the seller-beneficiary). For simplicity, this Comment excludes the business dealings between the buyer-applicant and third party-bank as representative of a third contract in the letter of credit transaction.

<sup>58</sup> Nobel Ins. Co. v. The First Nat'l Bank of Brundige, 821 So. 2d 210, 215 (Ala. 2001).

<sup>59</sup> *Id.*

<sup>60</sup> *Id.*

<sup>61</sup> U.C.C. § 5-102(a)(2) (1995); *see also* International Chamber of Commerce, *The Uniform Customs and Practice for Documentary Credits (UCP600)*, art. 2, ICC Publication No. 600 (July 1, 2007) [hereinafter UCP600] (defining *Applicant* as “the party on whose request the credit is issued.”).

<sup>62</sup> U.C.C. § 5-102(a)(9) (1995); *see also* UCP600, *supra* note 61 (defining *Issuing bank* as “the bank that issues a credit at the request of an applicant or on its own behalf.”).



specified in the letter of credit.<sup>63</sup> The letter of credit, therefore, is the second, overlying transaction, independent of the underlying transaction, and one that is between the issuing bank and seller or *Beneficiary*, called so because “under the terms of the letter of credit [he] is entitled to have its complying presentation honored.”<sup>64</sup> Once the seller-beneficiary presents the appropriate documentation to the third party-issuing bank, the bank pays the seller and then seeks reimbursement from the buyer-applicant.<sup>65</sup> The buyer then retrieves the seller’s goods and reimburses the bank.<sup>66</sup>

Primarily the U.C.C. or the Uniform Customs and Practice for Documentary Credits (UCP) govern choice of law and forum in U.S. letter of credit transactions. The UCP is propagated by the International Chamber of Commerce (I.C.C.) in Paris, France, and is not law.<sup>67</sup> However, given that the majority of financial institutions select the UCP as the governing framework of letter of credit transactions, the UCP has “the same binding effect as the law.”<sup>68</sup>

Revised U.C.C. § 5-116(c) defers the U.C.C. to the UCP. Parties will be governed by the UCP “to which the letter of credit, confirmation, or other undertaking is expressly made subject.”<sup>69</sup> Additionally, revised U.C.C. § 5-116(a) states that parties may choose the law governing the transaction, but that their decision must be mutually agreed upon.<sup>70</sup> The law of the chosen jurisdiction also “need not bear any relation to the transaction.”<sup>71</sup> Note, though, that just because parties select New York as

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<sup>63</sup> *Nobel Ins. Co.*, 821 So. 2d at 215.

<sup>64</sup> U.C.C. § 5-102(a)(3) (1995); *see, e.g.*, *New Orleans Brass, L.L.C. v. Whitney Nat'l Bank*, 818 So. 2d 1057, 1060 (La. Ct. App. 2002) (explaining “[i]n a letter of credit there are no less than three parties: an applicant (e.g. a buyer or lessee, etc.), an issuer (e.g. bank), and a beneficiary (e.g. a seller or lessor, etc.)”); *see also* UCP600, *supra* note 61 (defining *Beneficiary* as “the party in whose favour a credit is issued.”).

<sup>65</sup> *Nobel Ins. Co.*, 821 So. 2d at 215.

<sup>66</sup> *Id.*

<sup>67</sup> Franck Chantayan, Note, *Choice of Law Under Revised Article 5 of the Uniform Commercial Code - § 5-116*, 14 SAINT JOHN'S J. LEGAL COMMENT. 199, 206 (1999) (citing *E&H Partners v. Broadway Nat'l Bank*, 39 F. Supp. 2d 275, 281 (S.D.N.Y. 1998); *Calgarth Invs. Ltd. v. Bank Saderat Iran*, 1996 WL 204470, at \*7 (S.D.N.Y. Apr. 26, 1996), *aff'd*, 108 F.3d 329 (2d Cir. 1997) (unpublished table decision); *Mennen v. J.P. Morgan & Co., Inc.*, 653 N.Y.S.2d 1010, 1013 (A.D. 4th Dept. 1997)); *see also* LC RULES & LAWS, *supra* note 54, at 1 (UCP600 is promulgated by the Paris-based ICC).

<sup>68</sup> Chantayan, *supra* note 67, at 205-06.

<sup>69</sup> U.C.C. § 5-116(c) (1995).

<sup>70</sup> U.C.C. § 5-116(a) (1995); *see also* Chantayan, *supra* note 67, at 212 (stating that “[a]lthough the issuer generally makes the choice of law, under the existing law, [§] 5-116(a) of Revised Article 5 requires that both parties agree to the governing law.”).

<sup>71</sup> U.C.C. § 5-116(a) (1995).

their governing law, does not necessarily mean that the case will be tried in the New York forum. Therefore, coupled with § 5-116(a) is § 5-116(e), which holds that parties may choose the forum in the exact same manner as expressed for choice of law in § 5-116(a).<sup>72</sup> In application, subsection (e) can sometimes yield parties more power than the choice of law provision itself.<sup>73</sup> However, the most important subsection of § 5-116 is subsection (b). If parties do not reach agreement on law or forum, § 5-116(b) states that the law of the jurisdiction where the parties are located will govern the transaction.<sup>74</sup> Therefore, if an issuing bank has more than one branch—for example, one in Iran and another in New York<sup>75</sup>—the governing law will be from the jurisdiction where the branch that issues the letter of credit is located.<sup>76</sup>

## II. Analysis

The Comment's analysis proceeds in two sections. The first section explains why New York and international commercial transactions are synonymous with each other. The discussion merits a close reading of twentieth century financial history and the competition between London and New York, which subsequently made New York *New York*. This understanding is important because it helps to explain why courts began defending the interest of the New York forum, at least in part, as “overriding and paramount”<sup>77</sup> to the outcome of litigation. When a plaintiff argues that none of his contacts with the New York forum is more substantial than his vested presence in the market itself, he is persuading the New York court to hear litigation that could affect its own market.<sup>78</sup>

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<sup>72</sup> James E. Byrne, *Contracting Out of Revised U.C.C. Article 5 (Letters of Credit)*, 40 LOY. L.A. L. REV. 297, 307 (2006).

<sup>73</sup> *Id.*

<sup>74</sup> U.C.C. § 5-116(b) (1995); *see* Chantayan, *supra* note 67, at 212.

<sup>75</sup> *Calgarth Invs. Ltd. v. Bank Saderat Iran*, 1996 WL 204470, at \*1 (S.D.N.Y. Apr. 26, 1996) (Defendant Bank Saderat Iran, the state bank of Iran, which also managed a New York branch office, successfully moved to dismiss the action from the New York forum), *aff'd*, 108 F.3d 329 (2d Cir. 1997) (unpublished table decision).

<sup>76</sup> *Id.* (“BSI issued the first of the eight L/C's on December 1, 1992, and the last on October 31, 1993.”); *see also* Chantayan, *supra* note 67, at 212 (construing that “[i]n the event the issuing, advising or confirming bank has more than [sic] one branch, the governing law will be that of the jurisdiction of the branch that deals with the letter of credit transaction.”).

<sup>77</sup> *J. Zeevi & Sons, Ltd. v. Grindlays Bank (Uganda) Ltd.*, 37 N.Y.2d 220, 227 (1975) (citing *Intercontinental Planning, Ltd. v. Daystrom, Inc.*, 24 N.Y.2d 372, 383–84 (1969)).

<sup>78</sup> *See Auten v. Auten*, 308 N.Y. 155, 161 (1954) (“[T]he merit of its approach is that it gives to the place ‘having the most interest in the problem’ paramount control over the

Therefore, no other forum can be said to have a greater interest than New York. This perspective also sheds light on why New York courts sometimes perceive themselves as protectors of the “justified expectations”<sup>79</sup> of contracting parties.

The second section chips away at the centrality of the New York market. This section considers the American forum itself; that is, its popularity with foreign parties and courts’ response to this popularity. Today, commercial transactions commonly force courts to balance the interests of several legitimate forums.<sup>80</sup> The section considers alternative reactions to the forum race, such as forum pre-selection.<sup>81</sup> However, if parties do not reach agreement on law or forum, U.C.C. § 5-116(b) states that the law of the jurisdiction where the parties are located will govern the transaction.<sup>82</sup> In such cases, New York can be a tail end-finisher in a multi-forum race.<sup>83</sup> If the court does not grant the forum non conveniens motion, it could be faced with applying foreign law and inconveniencing parties and witnesses, for an action that has equal or greater interest in being heard overseas. Thus, melting before the court, from every direction, is a cluster of complex issues pointing toward applying the doctrine.

#### A. The New York Effect

*If I can make it there, I'll make it anywhere,  
It's up to you, New York, New York.*<sup>84</sup>

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legal issues arising out of a particular factual context, thus allowing the forum to apply the policy of the jurisdiction ‘most intimately concerned with the outcome of [the] particular litigation’ . . . .” (quoting Barbara Page, Note, *Choice of Law Problems in Direct Actions Against Indemnification Insurers*, 3 UTAH L. REV. 490, 498 (1952–1953)).

<sup>79</sup> *J. Zeevi & Sons*, 37 N.Y.2d at 227.

<sup>80</sup> See *Calgarth*, 1996 WL 204470, at \*7 (weighing the New York forum among five legitimate forums).

<sup>81</sup> See *infra* notes 116–19, 146–49 and accompanying text.

<sup>82</sup> U.C.C. § 5-116(b) (1995); see Chantayan, *supra* note 67, at 212.

<sup>83</sup> See, e.g., *Am. Express Bank Ltd. v. Banco Español de Crédito, S.A.*, 597 F. Supp. 2d 394, 399 (S.D.N.Y. 2009) (before dismissal from the New York forum, the court explained that the legal dispute “provoked legal proceedings in four jurisdictions: Switzerland, Spain, Pakistan, and the United States.”); *Calgarth*, 1996 WL 204470, at \*7 (holding that “New York arguably is no less convenient than Iran, as between inferior alternatives to any European forum, but this proves at best only that New York finishes fourth in a five-forum race.”).

<sup>84</sup> FRANK SINATRA, Theme Song from *New York, New York*, on TRILOGY: PAST, PRESENT, FUTURE (Reprise Records 1980).

The closing lines to Frank Sinatra's timeless song have renewed meaning in international commercial transactions. In the early 1920s, following the end of the First World War, European financial centers squandered to rehabilitate their international presence.<sup>85</sup> London, the world's pre-eminent financial center at the time, competed with New York in restoring control over the international gold standard.<sup>86</sup> Each city vied to be the major "reserve currency"<sup>87</sup> center, where foreign countries deposited their gold in exchange for interest-earning bills.<sup>88</sup> The reserve center then linked "the exchange system to gold by retaining its own reserves in that metal."<sup>89</sup> The result of all this strengthened the center's "balance-of-payments"<sup>90</sup> position and encouraged a dollar-sterling parity in favor of whatever city wore the hat.<sup>91</sup> For New York, the distinction was critical to gaining international economic prestige.<sup>92</sup> For London, the distinction was necessary to reclaiming its prestige.<sup>93</sup> Ultimately, a multitude of concerns<sup>94</sup> led Britain to overvalue the sterling by ten percent in relation to the dollar.<sup>95</sup> London's decision persuaded financial authorities in foreign countries to confer significant attention upon America's structuring of interest rates and prices, which quietly began transferring financial power to the shores of Manhattan.<sup>96</sup>

In the years that followed the changing of the guard, New York banks steadily increased their management of large volumes of international commercial transactions, because now their facilities and foreign connections were precisely adaptable to this field.<sup>97</sup> By the 1960s, the New York Court of Appeals accepted as common knowledge that New York City was "a national and international center for the purchase and sale of businesses and interests therein."<sup>98</sup> The court further interpreted state legislature as not protecting just state residents, but also foreigners who

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<sup>85</sup> See M.W. Kirby, *The Decline of British Economic Power Since 1870*, at 24–25, 37 (Routledge 2006) (1981).

<sup>86</sup> *Id.* at 37.

<sup>87</sup> *Id.*

<sup>88</sup> *Id.*

<sup>89</sup> *Id.*

<sup>90</sup> *Id.*

<sup>91</sup> *Id.*

<sup>92</sup> *Id.*

<sup>93</sup> *Id.*

<sup>94</sup> See generally *id.* at 24–43 (discussing Britain's return to the gold standard).

<sup>95</sup> *Id.* at 39–40.

<sup>96</sup> *Id.*

<sup>97</sup> 29 N.Y. Jur. 2d *Credit Cards and Letters of Credit* § 43 (2009).

<sup>98</sup> *Intercontinental Planning, Ltd. v. Daystrom, Inc.*, 24 N.Y.2d 372, 383 (1969).

utilized New York's market as a clearinghouse for international transactions.<sup>99</sup>

This is true because of all the jurisdictions involved, New York law affords the foreign principals the greatest degree of protection against the unfounded claims of brokers and finders. This encourages the use of New York brokers and finders by foreign principals and contributes to the economic development of our State. Our brokers and finders need only ensure that their agreements for compensation comply with the Statute of Frauds to receive the benefits of New York's position as a business center.<sup>100</sup>

Underneath this rationale was an inherent interest among New York courts to be the chosen forum for disputes arising out of New York's financial market.

This rationale hinged (and continues to hinge) on the sufficiency of contacts. For the courts, no contact was more sufficient than the presence of the financial market. New York was, and remains, "a financial capital of the world, serving as an international clearinghouse and market place for a plethora of international transactions."<sup>101</sup> Ignoring the presence of the market ignores the white elephant in the room, and the State has substantial interest in applying its policy to litigation that would affect its marketplace.<sup>102</sup> In fact, such an interest is "overriding and paramount"<sup>103</sup> in the outcome of litigation. Secondly, this interest is superseding on contractual foundations. After all, rooted in every transaction is a contract. A court that dismisses a forum non conveniens motion often cites to this simplicity, because it perceives its role as protecting the "justified expectations"<sup>104</sup> of the contracting parties.

In *Kossick v. United Fruit Co.*,<sup>105</sup> which involved a dispute over an alleged oral agreement, the U.S. Supreme Court held that the *where* is

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<sup>99</sup> *Id.* at 383–84.

<sup>100</sup> *Id.* at 384.

<sup>101</sup> *J. Zeevi & Sons*, 37 N.Y.2d at 227 (citing *Intercontinental Planning*, 24 N.Y.2d at 383–84).

<sup>102</sup> See cases cited *supra* note 6.

<sup>103</sup> *J. Zeevi & Sons*, 37 N.Y.2d at 227 (citing *Intercontinental Planning*, 24 N.Y.2d at 383–84).

<sup>104</sup> *Id.*

<sup>105</sup> 365 U.S. 731 (1961).

important to the extent that validity should be judged by the laws from wherever the agreement was made.<sup>106</sup>

Considering that sailors of any nationality may join a ship in any port, and that it is the clear duty of the ship to put into the first available port if this be necessary to provide prompt and adequate maintenance and cure to a seaman who falls ill during the voyage . . . it seems to us that this is such a contract as may well have been made anywhere in the world, and that the validity of it should be judged by one law wherever it was made.<sup>107</sup>

Cross-applying this holding to commercial transactions, a court would ask why a contract, that is born out of the benefits of the New York marketplace, should be denied the laws of New York.<sup>108</sup> What other forum could have greater interest and, thus, capture control of the resulting legal issues? The question is harder than it reads. Such are the beginnings of a melted court.

### B. The Melting Pot Effect

The melting pot is policy testing in a “substantial contacts” outfit. The New York Court of Appeals captures it as giving “to the place ‘having the most interest in the problem’ paramount control over the legal issues arising out of a particular factual context.”<sup>109</sup> The purpose is to determine which contact is the most substantial, but a simple mechanical formula is often suppressive.<sup>110</sup> In a commercial dispute, the court will likely be asked to balance the relative interests of several forums,<sup>111</sup> all of which may have equal or greater interest in applying their law over New York’s. As to this complexity, the U.S. Supreme Court explains:

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<sup>106</sup> *Id.* at 741.

<sup>107</sup> *Id.*

<sup>108</sup> *See, e.g., J. Zeevi & Sons*, 37 N.Y.2d at 227 (holding that “[s]ince New York has the greatest interest and is most intimately concerned with the outcome of this litigation, its laws should be accorded paramount control over the legal issues presented . . .”).

<sup>109</sup> *Auten v. Auten*, 308 N.Y. 155, 161 (1954) (citing *Page*, *supra* note 78).

<sup>110</sup> *See Vanston Bondholders Protective Comm. v. Green*, 329 U.S. 156, 161–62 (1946) (“In determining which contact is the most significant in a particular transaction, courts can seldom find a complete solution in the mechanical formulae of the conflicts of law.”).

<sup>111</sup> *Cf. Auten*, 308 N.Y. at 161 (explaining that a court’s weighing of significant contacts enables it “to reflect the relative interests of the several jurisdictions involved,” and to give the forum that is most interested in the action and the outcome of its litigation paramount control over the action. (citing *Vanston*, 329 U.S. at 161–62; *Page*, *supra* note 78)).

Certainly the part of this transaction which touched New York, namely, that the indenture contract was written, signed, and payable there, may be a reason why that state's law should govern. But apparently the bonds were sold to people all over the nation. And Kentucky's interest in having its own laws govern the obligation cannot be minimized. For the property mortgaged was there; the company's business was chiefly there; its products were widely distributed there; and the prices paid by Kentuckians for those products would depend, at least to some extent, on the stability of the company as affected by the carrying charges on its debts.<sup>112</sup>

Adding to this sentiment, the Southern District of New York has cited that the importance of its forum as a world financial capital does not alone deny a *forum non conveniens* motion.<sup>113</sup> Nor will “some tangential connection to New York”<sup>114</sup> merit a denial. The concern lies with using the connection, however minimal, as a trumpet to be played whenever a contracted party “seeks to use [American] courts for a lawsuit with little or no apparent contact with New York or the United States.”<sup>115</sup>

One solution that parties utilize, so as to avoid sounding like trumpets, goes back again to contractual basics. In *LaFarge Canada, Inc. v. Bank of China*,<sup>116</sup> the Southern District dismissed a *forum non conveniens* motion not because New York had vested interest in the litigation, but “because the parties selected ‘United States law’ to govern the contract.”<sup>117</sup> Therefore, the court was not burdened “with applying foreign law or dealing with complicated conflicts of law issues.”<sup>118</sup> This reasoning harkens back to courts’ perception of their roles as protecting the “justified expectations”<sup>119</sup> of the contracting parties.

However, it should be noted again that, per revised U.C.C. § 5-116(a), pre-selection of governing law does not automatically imply that the

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<sup>112</sup> *Vanston*, 329 U.S. at 162.

<sup>113</sup> *First Union Nat'l Bank v. Paribas*, 135 F. Supp. 2d 443, 453 (S.D.N.Y. 2001) (“[T]he existence of a letter of credit with some tangential connection to New York does not alone require the denial of a *forum non conveniens* dismissal . . .”).

<sup>114</sup> *Id.*

<sup>115</sup> *Id.*

<sup>116</sup> 2000 WL 1457012 (S.D.N.Y. Sept. 29, 2000).

<sup>117</sup> *Id.* at \*2.

<sup>118</sup> *Id.*

<sup>119</sup> *J. Zeevi & Sons*, 37 N.Y.2d at 227.

case will be tried in the jurisdiction whose law was chosen.<sup>120</sup> Rather, the important point of pre-selection is that, by specifically committing the contract to American law, parties legitimize their appearance before the bench. That is to say, parties who contract without selecting a governing law leave their fate in the hands of a backlogged and overburdened court. On the other hand, parties who pre-select New York as their governing law place less weight on their “tangential connection to New York,”<sup>121</sup> and also defer greater respect to their “justified expectations.”<sup>122</sup> Furthermore, parties’ pre-selection does not burden courts with having to (a) answer what foreign law applies, and then applying it, and (b) ironing out conflicts of law.<sup>123</sup>

Basically, all roads lead to New York because financial services represent “nearly the only thing left in which America still excels globally.”<sup>124</sup> Courts will deny a motion for forum non conveniens when the forum’s contacts are not simply substantial but *overriding* and, thus, must be recognized by the *forum’s* decisional law.<sup>125</sup> But perhaps, this country excels too well. Although New York has interest in the litigation, there is an equally important interest in preventing the forum from melting into an international court.<sup>126</sup> The fear is that applying foreign law to a plethora of

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<sup>120</sup> U.C.C. § 5-116(a) (1995).

<sup>121</sup> First Union Nat’l Bank v. Paribas, 135 F. Supp. 2d 443, 453 (S.D.N.Y. 2001).

<sup>122</sup> *J. Zeevi & Sons*, 37 N.Y.2d at 227.

<sup>123</sup> *LaFarge*, 2000 WL 1457012, at \*4.

<sup>124</sup> George Steven Swan, *The Law and Economics of Interprofessional Frontier Skirmishing*: Financial Planning Association v. Securities and Exchange Commission, 16 U. MIAMI BUS. L. REV. 75, 89 (2007). To be more specific, it can be argued that all roads lead to New York because the medium for payment of reserve currencies is in United States dollars. In the event of legal action, the dollar transaction allows parties to sink a hook into the New York market. *See, e.g.*, Hanil Bank v. PT. Bank Negara Indonesia (Persero), 148 F.3d 127, 130 (2d Cir. 1998) (plaintiff instructed defendant in Indonesia to remit payment owed to it under the letter of credit in United States dollars to its New York account); *J. Zeevi & Sons*, 37 N.Y.2d at 227 (holding that “[t]he parties, by listing United States dollars as the form of payment, impliedly . . . set up procedures to implement their trust in our policies.”).

<sup>125</sup> *See J. Zeevi & Sons*, 37 N.Y.2d at 227 (New York “is a financial capital of the world, serving as an international clearinghouse and market place for a plethora of international transactions, such as to be so recognized by our decisional law”).

<sup>126</sup> *See, e.g.*, *Verlinden B.V. v. Cent. Bank of Nigeria*, 461 U.S. at 480, 490 (1983) (citing to Jurisdiction of U.S. Courts in Suits Against Foreign States: Hearings Before the Subcomm. on Admin. Law and Governmental Relations of the H. Comm. on the Judiciary on H.R. 11315, 94th Cong. 31 (1976) (testimony of Brunon A. Ristau) (“The bill is not designed to open up our courts to all comers to litigate any dispute which any private party may have with a foreign state anywhere in the world”)); *Calgarth Invs. Ltd. v. Bank Saderat Iran*, 1996 WL 204470, at \*7 (S.D.N.Y. Apr. 26, 1996) (concluding that “New



sufficient actions will be as harmful to the forum as dismissing one necessary action. The applications will maximize inefficiency, burden the court, and distract it from transactions that will actually affect the forum.

In a letter of credit transaction, the parties are usually sophisticated corporations. The underlying transaction might engage an American corporation with a foreign entity in continuous international dealings.<sup>127</sup> Suppose, too, that the American corporation is capable of assuming the burdens attached to litigating in a foreign forum.<sup>128</sup> Professor Mary Kay Kane admits that courts may be less quick to grant a forum non conveniens motion when the only alternative forum exists in a foreign country.<sup>129</sup> However, she counters that courts should not dismiss this motion “without undertaking a careful analysis of the facts as they relate to the actual convenience of those [parties] involved.”<sup>130</sup>

For example, in *Calgarth Investments Ltd. v. Bank Saderat Iran*,<sup>131</sup> Calgarth Investments, an Irish corporation headquartered in London, sued Bank Saderat Iran (BSI), the state bank of Iran, and its New York branch (BSI-NY), for wrongful dishonor of eight documentary letters of credit.<sup>132</sup> Under the terms of the credits, BSI issued them in dollar currency payable at Ceskoslovenska Obchodni Bank, A.S. (COB), a Czech bank located in Prague and the de facto advising and negotiating bank.<sup>133</sup> Strojimport Foreign Trade Co. (Stroji), a Czech corporation, transferred its rights as beneficiary to Calgarth under an agreement providing that terms would be subject to the Obligations Law of Switzerland.<sup>134</sup> However, when Calgarth requested payment from BSI-NY, BSI refused.<sup>135</sup> Stroji had informed BSI that its assignment to Calgarth stopped being valid after Calgarth failed to

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York [finished] fourth in a five-race forum”), *aff'd*, 108 F.3d 329 (2d Cir. 1997) (unpublished table decision).

<sup>127</sup> See Mary Kay Kane, *Suing Foreign Sovereigns: A Procedural Compass*, 34 STAN. L. REV. 385, 412 (1982) (“[T]hese concerns do not always compel denial of dismissal as, for example, when the plaintiff is an American corporation engaged in a continuous international business and is fully capable of assuming the burdens of litigating in a foreign forum.”).

<sup>128</sup> *Id.*

<sup>129</sup> *Id.*

<sup>130</sup> *Id.*

<sup>131</sup> 1996 WL 204470 (S.D.N.Y. Apr. 26, 1996), *aff'd*, 108 F.3d 329 (2d Cir. 1997) (unpublished table decision).

<sup>132</sup> *Id.* at \*1.

<sup>133</sup> *Id.*

<sup>134</sup> *Id.*

<sup>135</sup> *Id.* at \*1–2.

perform contractual obligations.<sup>136</sup> When Calgarth sued BSI and BSI-NY for wrongful dishonor, defendants moved to dismiss under sovereign immunity and forum non conveniens.<sup>137</sup>

The Southern District of New York recognized the *Piper* holding when it stated that substantially less deference would be given to a foreign plaintiff who brought suit in an American forum, because his choice, by its very nature, less reasonably assumed that he chose the forum out of convenience.<sup>138</sup> The court, finding inconvenience instead, explained as follows:

This lawsuit arises from events occurring primarily in the Czech Republic. The important characters in the story reside in the Czech Republic, Iran, and England, far from the United States. The law that will determine the competing rights of Calgarth and BSI . . . is the Obligations Law of Switzerland. The court is unable to identify any interest this jurisdiction holds in the present controversy, other than that a trial here would generate revenue for the New York hotels and restaurants that would host inconvenienced witnesses forced to travel here from England, Iran, and the Czech Republic. But that interest is not a public interest in the “outcome of the litigation.”<sup>139</sup>

It was not that Calgarth had established insufficient contacts to legitimize the New York forum; it was that the other forums were more appropriate and that, at best, “New York [finished] fourth in a five-forum race.”<sup>140</sup>

Under Professor Kane’s analysis, the fact that BSI represented the state would be additional fodder for denying the motion, but principally if Calgarth were an American corporation.<sup>141</sup> Following the adoption of the Foreign Services Immunities Act (FSIA) in 1976,<sup>142</sup> American plaintiffs

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<sup>136</sup> *Id.* at \*1.

<sup>137</sup> *Id.* at \* 2.

<sup>138</sup> *Id.* at \*5 (citing *Piper Aircraft Co. v. Reyno*, 454 U.S. 235, 255–56 (1981)).

<sup>139</sup> *Id.* at \*7.

<sup>140</sup> *Id.*

<sup>141</sup> Kane, *supra* note 127 (“The fact that the defendant is a foreign government raises additional concerns that argue against dismissal.”).

<sup>142</sup> 28 U.S.C. § 1330. The Act gives district courts original jurisdiction, regardless of the amount in controversy, in any civil bench action against a foreign state “as to any claim for relief in personam with respect to which the foreign state is not entitled to immunity,” 28 U.S.C. § 1330(a).

had the right to sue foreign states in American courts.<sup>143</sup> This policy inherently favored a plaintiff's choice of an American forum over a foreign one when evidence suggested that fairness and impartiality would be compromised abroad.<sup>144</sup> The presence of a defendant-state will not mechanically deny a motion of forum non conveniens; however, as Kane suggests, the presence will more likely oblige courts to raise standards for granting defendant's motion.<sup>145</sup>

Moreover, if parties in *Calgarth* explicitly contracted to be governed by American law, regardless of their foreign allegiance, the Southern District would have been harder pressed to grant defendants' motion. For example, in *Eckert International v. Government of Sovereign Democratic Republic of Fiji*,<sup>146</sup> the Fourth Circuit recognized that the contracting parties—a Virginia corporation and the government of Fiji—clearly intended for Virginia to be the forum when they drafted a specific agreement attesting to this preference.<sup>147</sup> Generally, the FSIA recognizes waivers of sovereign immunity where a foreign state agrees to arbitrate in another country; or agrees that the law of a particular country will govern the contract; or files a responsive pleading in a suit without raising a defense of sovereign immunity.<sup>148</sup> Here, by entering into a contract with a Virginia corporation, which included the aforesaid choice of law provision, Fiji very plainly intended to waive its immunity.<sup>149</sup>

In *Calgarth*, BSI moved to dismiss the New York action on grounds of sovereign immunity and forum non conveniens.<sup>150</sup> The dual motion meant that before the court could dismiss the action by forum non conveniens, it had to address subject-matter jurisdiction.<sup>151</sup> Specifically, the court answered whether BSI was subject to suit under its waiver of

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<sup>143</sup> Kane, *supra* note 127.

<sup>144</sup> *Id.* (“Given this policy, the presumption favoring [an American] plaintiff's choice of an American tribunal over a foreign one seems even stronger than in other types of actions, especially when there is reason for concern about the fairness or impartiality of litigating against a foreign state in its own tribunals.”).

<sup>145</sup> *Id.*

<sup>146</sup> 32 F.3d 77 (4th Cir. 1994).

<sup>147</sup> *Id.* at 80; *see also* Joseph v. Office of Consulate Gen. of Nigeria, 830 F.2d 1018, 1022 (9th Cir. 1987) (holding that “a sovereign party has waived immunity where a contract *specifically* states that the laws of a jurisdiction within the United States are to govern the transaction.”).

<sup>148</sup> *Id.* at 79 (citing 28 U.S.C. § 1605).

<sup>149</sup> *Id.* at 77.

<sup>150</sup> *Calgarth Invs. Ltd. v. Bank Saderat Iran*, 1996 WL 204470, at \*2 (S.D.N.Y. Apr. 26, 1996), *aff'd*, 108 F.3d 329 (2d Cir. 1997) (unpublished table decision).

<sup>151</sup> *Id.*

immunity in an international agreement<sup>152</sup> or, if it was not, whether the FSIA's *commercial activity* provision exempted BSI.<sup>153</sup> Had *Calgarth* been tried today, the court could have sidestepped subject-matter jurisdiction and, instead, cited to *Sinochem International Co. v. Malaysia International Shipping Corp.*<sup>154</sup> *Sinochem* arose out of a letter of credit transaction, and the procedural holding by the U.S. Supreme Court is broadly valuable: A district court "may dispose of an action by a *forum non conveniens* dismissal, bypassing questions of subject-matter and personal jurisdiction, when considerations of convenience, fairness, and judicial economy so warrant."<sup>155</sup>

The seller, Trorient Trading, Inc., sub-chartered a vessel from Malaysia International for transport of steel coils to the buyer, Sinochem International (a Chinese state-owned importer).<sup>156</sup> Under the terms of the letter of credit, Trorient would be paid after it produced to the Issuer "a valid bill of lading certifying that the coils had been loaded for shipment [from Philadelphia] to China on or before [a specified date]."<sup>157</sup> Sinochem later alleged that Malaysia falsely backdated the bill of lading, resulting in Sinochem's unwarranted payment under the letter of credit.<sup>158</sup> Sinochem petitioned a Chinese admiralty court to arrest the vessel, but before the court could act, Malaysia filed a concomitant action in federal district court.<sup>159</sup> The complaint asserted that Sinochem's petition to the admiralty court negligently misrepresented Malaysia's reliability to transport steel coils.<sup>160</sup> Sinochem motioned for dismissal under (1) lack of subject matter jurisdiction; (2) lack of personal jurisdiction; (3) international comity; and (4) *forum non conveniens*.<sup>161</sup>

The Court, citing from the Seventh Circuit, characterized jurisdiction as "vital only if the court proposes to issue a judgment on the

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<sup>152</sup> *Id.* at \*3–5. After exhaustive consideration, the court concluded that BSI was "subject to suit on the basis of consent under an international agreement," *id.* at 5.

<sup>153</sup> *Id.* at \*3 (citing 28 U.S.C. § 1605(a)(2)). The *commercial activity* provision provides that a foreign state will not be immune to United States jurisdiction in any case where "the action is based upon a commercial activity carried on in the United States by the foreign state," 28 U.S.C. § 1605(a)(2).

<sup>154</sup> 549 U.S. 422 (2007).

<sup>155</sup> *Id.* at 423.

<sup>156</sup> *Id.* at 426.

<sup>157</sup> *Id.*

<sup>158</sup> *Id.*

<sup>159</sup> *Id.* at 427.

<sup>160</sup> *Id.*

<sup>161</sup> *Id.*

merits.”<sup>162</sup> Dismissal of an action on the ground of forum non conveniens “is a determination that the merits should be adjudicated elsewhere.”<sup>163</sup> Therefore, it is not necessary for a court to consider questions of subject matter or personal jurisdiction, if the court has already determined that another forum is better suited to hear the merits of the case.<sup>164</sup>

Comparably, *American Express Bank Ltd. v. Banco Español de Crédito, S.A.*<sup>165</sup> reinforces the *Sinochem* holding that an action belongs in an appropriate forum, and questions as to the chosen forum’s adequacy should be among the very first that the court answers. *American Express* also underscores the *Calgarth* complexity of the forum in letter of credit litigation. The transaction at issue involved four parties spanning across four foreign jurisdictions—Switzerland, Spain, Pakistan, and the United States (Southern District of New York).<sup>166</sup> In this forum race, the United States finished last,<sup>167</sup> but the facts strongly suggested that the action had no business whatsoever of even being tried in a United States forum. That is why the most puzzling aspect of the court’s decision was that it did not at all turn on forum non conveniens.

The parties in the underlying contract, Isolux (a Spanish engineering firm) and the Pakistan Water and Power Development Authority (WAPDA), expressly agreed that in the event of a dispute, they would submit their claims to the I.C.C. International Court of Arbitration in Switzerland, where “[t]he award of the majority of the [arbitrators] [would] be final and binding on both parties.”<sup>168</sup> At WAPDA’s request, Isolux also obtained two demand guarantees, which are commonly used in international construction contracts and “provide a simple way for a buyer to obtain cash for substitute performance if a contractor defaults.”<sup>169</sup> The Pakistani branch of American Express Bank (AEB) executed guarantees in favor of WAPDA, while Banco Español de Crédito (Banesto) issued counter-

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<sup>162</sup> *Id.* (quoting *Intec USA, LLC v. Engle*, 467 F.3d 1038, 1041 (7th Cir. 2006)).

<sup>163</sup> *Id.* at 432 (citing *Am. Dredging Co. v. Miller*, 510 U.S. 443, 454 (1994); *Chick Kam Choo v. Exxon Corp.*, 486 U.S. 140, 148 (1988)).

<sup>164</sup> *Id.* at 425.

<sup>165</sup> 597 F. Supp. 2d 394 (S.D.N.Y. 2009).

<sup>166</sup> *Id.* at 399.

<sup>167</sup> *Id.* at 396 (dismissing AEB’s complaint without prejudice “to the filing of a new action following further developments in Pakistan.”).

<sup>168</sup> *Id.* at 397.

<sup>169</sup> *Id.* (citing David J. Barru, *How to Guarantee Contractor Performance on International Construction Projects: Comparing Surety Bonds with Bank Guarantees and Standby Letters of Credit*, 37 GEO. WASH. INT’L L. REV. 51 (2005)).

guarantees in AEB's favor in the event that AEB incurred liability under the guarantees.<sup>170</sup>

Details of the underlying contractual disputes between Isolux's performance and WAPDA's payment obligations are not relevant to this analysis. What matters first is that the disputes provoked legal proceedings in multiple forums.<sup>171</sup> What matters second is that, in light of the facts provided, the action filed in the Southern District did not turn foremost on forum non conveniens.<sup>172</sup> In the first legal proceeding, which was requested by Isolux, the I.C.C. arbitral tribunal ordered WAPDA to cancel the guarantees and pay Isolux approximately U.S. \$788,066.<sup>173</sup> This decision and award was "final and binding as a matter of Swiss law upon notification to the parties."<sup>174</sup> In the second proceeding, Isolux concurrently obtained an injunction from a Spanish court (1) enjoining WAPDA from demanding payment on AEB's guarantees and (2) instructing Banesto to dishonor any requests for payment of guarantees or counter-guarantees.<sup>175</sup> In the third proceeding, but contrary to the arbitral decision against it, WAPDA sued AEB in Pakistan to recover against alleged wrongful dishonor of the guarantees.<sup>176</sup> Coupled with this action was a fourth proceeding, filed in the Southern District, wherein AEB insisted that Banesto pay out the counter-guarantees, despite that AEB had not paid the guarantees to WAPDA.<sup>177</sup> To establish contact with New York, AEB cited to Banesto's office there, as well as to an account agreement executed with AEB New York:

Banesto is already present in this jurisdiction. It has an office for the regular transaction of business at 521 Fifth Avenue, New York, New York. Banesto's relationship with American Express is centered in New York, governed by the New York Account Agreement. Since at least 1980, Banesto has maintained an account with American Express in New York, and the terms of that account (the Account Agreement), serve

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<sup>170</sup> *Id.* at 397–98.

<sup>171</sup> *Id.* at 399.

<sup>172</sup> *See id.* at 401 (“[T]here is no need to resolve [the choice of forum law] now. The complaint and the three memoranda of law submitted by AEB assume that New York law applies. If the complaint does not state a claim under New York law, it necessarily fails to state a claim upon which relief can be granted and Banesto's motion to dismiss must be granted.”).

<sup>173</sup> *Id.* at 400.

<sup>174</sup> *Id.*

<sup>175</sup> *Id.* at 399.

<sup>176</sup> *Id.*

<sup>177</sup> *Id.* at 399–400.

as an umbrella agreement governing the global relations of the parties. Accordingly, there is a *bona fide* connection between this forum and the parties and this dispute. As such, plaintiff's choice of forum in its home forum should be given great deference.<sup>178</sup> (Textual footnotes excluded.)

The Southern District, however, did not resolve AEB's choices of forum and law and, instead, assumed New York applied.<sup>179</sup> That is to say, the court held that AEB's complaint did not state a claim under New York law upon which declaratory relief could be granted.<sup>180</sup> The court thus granted Banesto's Rule 12(b)(6) motion.<sup>181</sup>

What remains troubling, though, is that an action never reasonably belonged in a United States forum. Applying *Calgarth* reasoning, AEB's suit in New York arose out of events that occurred in Pakistan, by parties who resided in Pakistan and Spain, as well as arbitration that occurred in Switzerland under Swiss law.<sup>182</sup> In its Memorandum in Support of the Motion to Dismiss, Banesto highlighted that:

[N]ot a single event giving rise to this action took place in New York. The sole, tangential connection of this case to New York [was] the fact that AEB Pakistan's corporate parent [was] headquartered there. That fact deserves little weight, however, given that the transactions at issue involved AEB's Pakistani branch, rather than the corporate parent. AEB emphasizes that Banesto operates a New York branch . . . but that branch had nothing to do with the transactions at issue, which entirely involved Banesto Madrid.<sup>183</sup>

Second, AEB's request for declaratory relief wholly relied on assumptions that the Pakistani proceeding would (1) rule for WAPDA (2) in a way that required AEB to pay WAPDA's guarantees, and (3) also triggered Banesto's duty to pay AEB's counter-guarantees.<sup>184</sup> Finally, the Spanish proceeding,

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<sup>178</sup> Plaintiff's Memorandum in Support of Motion for Summary Judgment at 19-20, *Am. Express Bank*, 597 F. Supp. 2d at 401 (No. 06 CV 3484).

<sup>179</sup> *Am. Express Bank*, 597 F. Supp. 2d at 401. See parenthetical explanation cited *supra* note 167.

<sup>180</sup> *Id.* at 405.

<sup>181</sup> *Id.* at 406.

<sup>182</sup> See *supra* notes 139, 165-77 and accompanying text.

<sup>183</sup> Defendant's Memorandum in Support of Motion to Dismiss at 27, *Am. Express Bank*, 597 F. Supp. 2d at 401 (No. 06 CV 3484).

<sup>184</sup> *Am. Express Bank*, 597 F. Supp. 2d at 406.

whose injunction prohibited Banesto from honoring counter-guarantees, already estopped AEB's request.<sup>185</sup> Because Banesto was already subject to this forum, for the matter at issue, Spain was an adequate alternative to AEB's inadequate forum selection.<sup>186</sup>

### Conclusion

Consider John and Jane's hypothetical transaction from the introduction. Indeed, as commercial transactions like this one grow increasingly international,<sup>187</sup> forum non conveniens will grow increasingly important for litigators. This Comment introduced the contours of forum non conveniens in letter of credit litigation. The case law discussed revealed two general attitudes that courts embrace, in whole or in part, when they are confronted by this type of litigation: (1) for denying (or dismissing) the application of forum non conveniens, because the court's forum, and thus its financial market, has superseding interest in the letter of credit litigation;<sup>188</sup> or (2) for granting (or upholding) the application of forum non conveniens, because the limited contacts presented by plaintiff would otherwise open a flood gate and turn the forum into a melting pot for complex foreign issues.<sup>189</sup>

The financial backdrop of a forum, at least in part, can induce courts to protect litigation from being heard in alternative forums. However, if a foreign plaintiff, like John (but, perhaps, with more disposable resources), can cite only a "tangential connection to New York,"<sup>190</sup> then any argument boasting the forum's need to hear the action, simply because of its financial milieu, should fail.<sup>191</sup> Moreover, John has to question whether it is in his best interest to elevate even legitimate contacts to New York, to sue ABC there, and then return to his home forum in Macau and try to enforce a favorable decision. Alternatively, if John and ABC pre-selected New York as their governing law, John ends up placing less weight on his connections,

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<sup>185</sup> *Id.* at 399.

<sup>186</sup> Defendant's Memorandum in Support of Motion to Dismiss at 28, *Am. Express Bank*, 597 F. Supp. 2d at 401 (No. 06 CV 3484) ("Banesto has already been subjected to a Spanish court injunction relating to the Counter-Guarantees at issue in this case. Because Banesto is subject to suit in Spain and a cause of action for breach of contract is available there, Spain is clearly an adequate alternative forum for this litigation." (citing *Pollux Holding Ltd. v. Chase Manhattan Bank*, 329 F.3d 64, 75 (2d Cir. 2003))).

<sup>187</sup> Hicks, *supra* note 1.

<sup>188</sup> See cases cited *supra* note 6.

<sup>189</sup> See cases cited *supra* note 126.

<sup>190</sup> *First Union Nat'l Bank v. Paribas*, 135 F. Supp. 2d 443, 453 (S.D.N.Y. 2001).

<sup>191</sup> See *supra* note 139 and accompanying text.



and also invokes greater respect for both parties' "justified expectations."<sup>192</sup> Revised U.C.C. § 5-116(a) holds that pre-selection does not assume the case will be heard in the New York forum.<sup>193</sup> If both parties are insistent on this forum, then they must pre-select it under § 5-116(e).<sup>194</sup> At least from a court's perspective, though, the best test for locating the appropriate forum in letter of credit litigation is under § 5-116(b), which states that, without an agreement, the law of the jurisdiction where the Issuer is located will govern the transaction.<sup>195</sup> As in *Calgarth*, where the Issuer had two addresses, one in Iran and one in New York,<sup>196</sup> the address where the undertaking was issued mattered most.<sup>197</sup> If *Calgarth* had shown that the undertaking was instead issued at BSI's New York branch, or that the New York branch was intimate enough with the issuance or management of the letter of credit, then it would become a powerful § 5-116(b) argument.

The plaintiff's hurdles arise in full force when defendant can show that facts primarily occurred in a foreign country by mostly foreign participants, and when the court must choose which among several legitimate is the most applicable. Melting before the court is a cluster of complex issues. If the court does not grant the forum non conveniens motion, it could be faced with applying foreign law and inconveniencing parties and witnesses, for an action that has equal or greater interest in being heard overseas.

Traditionally, American courts show substantially less deference to foreign plaintiffs that bring suit in an American forum, because the choice, by its very nature, assumes that plaintiff chose the forum for reasons other than convenience.<sup>198</sup> However, less deference still implies *some* deference.<sup>199</sup> Foreign plaintiffs must be mindful that it is usually not enough to *just* establish sufficient contacts in the New York forum.<sup>200</sup> More important for courts is whether other legitimate forums are better suited to

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<sup>192</sup> *J. Zeevi & Sons*, 37 N.Y.2d at 227.

<sup>193</sup> U.C.C. § 5-116(a) (1995).

<sup>194</sup> U.C.C. § 5-116(e) (1995).

<sup>195</sup> U.C.C. § 5-116(b) (1995); see Chantayan, *supra* note 67, at 212.

<sup>196</sup> *Calgarth Invs. Ltd. v. Bank Saderat Iran*, 1996 WL 204470, at \*1 (S.D.N.Y. Apr. 26, 1996), *aff'd*, 108 F.3d 329 (2d Cir. 1997) (unpublished table decision).

<sup>197</sup> *Id.* ("BSI issued the first of the eight L/C's on December 1, 1992, and the last on October 31, 1993."); see U.C.C. § 5-116(b) (1995) ("If more than one address is indicated, the person is considered to be located at the address from which the person's undertaking was issued.").

<sup>198</sup> *Calgarth*, 1996 WL 204470, at \*5 (citing *Piper Aircraft Co. v. Reyno*, 454 U.S. 235, 255-56 (1981)).

<sup>199</sup> *Ravelo Monegro v. Rosa*, 211 F.3d 509, 514 (9th Cir. 2000); see *Lear*, *supra* note 41.

<sup>200</sup> *Calgarth*, 1996 WL 204470, at \*7.

hear the action, apply relevant law, and conveniently cater to parties and witnesses.<sup>201</sup> Courts' discretionary power here, under the doctrine of forum non conveniens, is a calculated unpredictability. However, this does not lessen the fact that New York remains a mecca for substantial sums of international letter of credit business. If a party truly wishes to have his action decided in New York, then he will be wise to consider this analysis before framing his transaction.

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<sup>201</sup> *Id.* (Switzerland and England “would be vastly more convenient than New York. New York arguably is no less convenient than Iran, as between inferior alternatives to any European forum, but this proves at best only that New York finishes fourth in a five-forum race.”).

**What Constitutes an *Original* Letter of Credit in the Fifth Circuit?  
*LaBarge: America's Glencore***

Matthew Butsick<sup>†</sup>

**Introduction**

The International Chamber of Commerce's (ICC) Uniform Customs and Practices for Documentary Credits (UCP) is one of the primary sets of rules relied upon for governance of letter of credit transactions.<sup>1</sup> Not only has the ICC produced several revisions of the UCP since its inception, but experts, legal scholars, and bankers have written countless books, brochures, manuals, treatises, academic papers, and court decisions on the topic. Even the ICC itself has issued opinions to clarify and expound the meaning of the UCP's text. In sum, a plethora of material is available to help an interested party understand these rules. So, if a question arose as to what the UCP drafters meant by the use of a technical term, naturally, one would turn to . . . a dictionary? The court in *LaBarge Pipe & Steel Co. v. First Bank*,<sup>2</sup> did so, defining and interpreting the UCP terms "original" and "operative instrument" in ways that seriously distorted the meanings of the terms and misinterpreted provisions of the UCP.

In *LaBarge*,<sup>3</sup> PVF USA, LLC requested that First Bank issue a letter of credit for US\$144,000,000 in favor of LaBarge Pipe & Steel Co. as payment for the sale of steel pipe.<sup>4</sup> Accordingly, First Bank sent its letter of credit via telefax with a cover sheet stating, "Here is the letter of credit you requested. Please let me know if you need any additional information."<sup>5</sup> LaBarge's employee requested a change in the terms stipulated in the telefaxed letter of credit, First Bank sent an amended letter of credit via telefax along with a cover sheet stating, "Here is the revision to the letter of credit you requested. Please let me know if you need any additional

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<sup>1</sup> James E. Byrne, *Editor's Overview* to International Chamber of Commerce, *The Uniform Customs and Practice for Documentary Credits (UCP600)*, ICC Publication No. 600 (July 1, 2007), in *LC RULES & LAWS CRITICAL TEXTS 1* (James E. Byrne ed., 4th ed. 2007).

<sup>2</sup> *LaBarge Pipe & Steel Co. v. First Bank*, 550 F.3d 442 (5th Cir. 2008).

<sup>3</sup> *Id.*

<sup>4</sup> *Id.* at 446.

<sup>5</sup> *Id.*

information.”<sup>6</sup> Nowhere did the telefaxed cover sheet or the text of the undertaking state that “full details [were] to follow” or a similar statement.<sup>7</sup>

The terms of the letter of credit, among other things, required that the *original* letter of credit be presented to its issuer.<sup>8</sup> The Fifth Circuit, relying on *Black’s Law Dictionary*<sup>9</sup> rather than practice, defined “original” as the “first copy of the document.”<sup>10</sup> Therefore, the court ruled that when LaBarge Pipe & Steel Co. submitted the telefaxed, amended letter of credit in its presentation to First Bank, the presentation did not comply with the terms required in the letter of credit.<sup>11</sup>

This article will analyze the decision in *LaBarge*. To do so, it will revisit the drafting history of relevant provisions of the UCP, consider the meaning and role of originality in letter of credit law as well as practice, and review relevant case law. In light of this background, this article will then analyze the decision in *LaBarge* and show it to be inconsistent with the intent of the general banking community.

## I. Background

Essential to understanding the outcome in *LaBarge* is a brief background of the relevant points of letter of credit law and banking practice. These include the following, which are indispensable for proceeding: the scope and purpose of letters of credit, what is meant by the terms “documentary credit” and “original documents,” an understanding of the level of scrutiny applied by banks to documents presented, the application of the concept of ambiguity, and the time when a letter of credit becomes available.

### A. Brief Explanation of the Field

The primary role of a letter of credit is to serve as a method of payment or source of potential payment in relation to an underlying transaction.<sup>12</sup> The basic letter of credit transaction involves three undertakings: an application (between the applicant and issuer), a letter of

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<sup>6</sup> *Id.*

<sup>7</sup> *Id.*

<sup>8</sup> *Id.* at 451.

<sup>9</sup> BLACK’S LAW DICTIONARY 1099 (6th ed. 1990).

<sup>10</sup> *LaBarge*, 550 F.3d at 452-53.

<sup>11</sup> *Id.* at 453.

<sup>12</sup> BORIS KOZOLCHYK, COMMERCIAL LETTERS OF CREDIT IN THE AMERICAS 7-10 (1966).

credit (between the issuer and beneficiary), and an underlying contract (between the beneficiary and applicant).<sup>13</sup> The Louisiana Revised Statutes attempt to explain the relationship in §10:5-102(a)(10), defining a letter of credit as “a definite undertaking that satisfies the [formal requirements] by an issuer to a beneficiary at the request or for the account of an applicant or, in the case of a financial institution, to itself or for its own account, to honor a documentary presentation by payment or delivery of an item of value.”<sup>14</sup>

The purpose of a letter of credit is to “relieve the tension between merchants and buyers when the merchant is hesitant to lose possession of its goods before being paid, but the buyer would like to have the goods before parting with its money.”<sup>15</sup> Through the use of a letter of credit, the overall amount of risk is reduced, eliminating some of the transaction costs that would otherwise be incurred by all parties to satisfy a beneficiary’s risk-averse nature.<sup>16</sup> Parties use letters of credit rather than other payment means for many reasons, but generally they use commercial letters of credit primarily to reduce the risk associated with both international and domestic sales of goods,<sup>17</sup> while they use standby letters of credit to assure a party’s payment or performance through a third party promise to pay.<sup>18</sup>

The nature of a letter of credit obligation is documentary in character.<sup>19</sup> In order to receive payment, beneficiaries must first present documents specified in the letter of credit to the issuing bank.<sup>20</sup> When presentation of documents is made under a letter of credit, the default “rule is and always has been that original documents are required.”<sup>21</sup> The purpose behind such a requirement is that the original may have a “particular commercial, legal or evidential value” for the parties involved.<sup>22</sup>

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<sup>13</sup> *Id.*

<sup>14</sup> LA. REV. STAT. ANN. §10:5-110(a)(10) (2003).

<sup>15</sup> *LaBarge*, 550 F.3d at 449 (citing JAMES J. WHITE & ROBERT S. SUMMERS, UNIFORM COMMERCIAL CODE §26-1 (5th ed. 2008)).

<sup>16</sup> KOZOLCHYK, *supra* note 12, at 9.

<sup>17</sup> *Id.* at 9-12.

<sup>18</sup> *LaBarge*, 550 F.3d at 450 (citing JAMES J. WHITE & ROBERT S. SUMMERS, UNIFORM COMMERCIAL CODE §26-1(b) (5th ed. 2008)).

<sup>19</sup> KOZOLCHYK, *supra* note 12, at 8-9.

<sup>20</sup> *Id.*

<sup>21</sup> Adam Johnson, *Letters of Credit and Original Documents-Again*, 14 J.I.B.L. 287 (1999) (citing RAYMOND JACK, DOCUMENTARY CREDITS 161 (1993) (1991)).

<sup>22</sup> RAYMOND JACK, DOCUMENTARY CREDITS 153 (Ali Malek QC & David Quest eds., 2009) (1991).

Under standard international practice, and as provided in the Uniform Customs and Practice 400 (UCP400), banks will accept documents “as presented, provided that they appear on their face to be in accordance with the other terms and conditions of the credit.”<sup>23</sup> Embedded within this standard is the doctrine of strict compliance, which stipulates that the documentation presented by a beneficiary of a letter of credit must “comply exactly with the requirements of the credit;” otherwise, the issuer may dishonor.<sup>24</sup> In the field of letter of credit practice, because of the reliance on documentary terms and conditions, certain words and phrases take on special meanings as terms of art. Generally, the default rule in letter of credit law is that ambiguity is held against the drafter of the document.<sup>25</sup> Therefore, in order to strictly comply with the terms of the standby, a beneficiary would need to present “the original Irrevocable Letter of Credit,” as stipulated in the standby.<sup>26</sup>

Once a letter of credit is sent or otherwise transmitted to the beneficiary or advising party, it is deemed to be “issued and becomes enforceable according to its terms against the issuer.”<sup>27</sup> Credits can be issued in several formats, one of which is the *teletransmission* credit. A teletransmission credit is a credit that is transmitted electronically, typically by cable, telegram, telex, or facsimile, and can later be evidenced in paper form.<sup>28</sup>

### B. Evolution of Concept of Original

After World War I, the international banking community found itself in need of an “authoritative and consistent formulation” to promote uniformity in letter of credit practice.<sup>29</sup> In 1929, the International Chamber of Commerce published a set of rules, which by 1933 had evolved into the first UCP.<sup>30</sup> An early description of the UCP was a “semi-official international codifications of customs.”<sup>31</sup> In *LaBarge*, the letter of credit at

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<sup>23</sup> International Chamber of Commerce, *The Uniform Customs and Practice for Documentary Credits (UCP400)*, art. 22, ICC Publication No. 400 (Oct. 1, 1984) [hereinafter UCP400].

<sup>24</sup> *LaBarge*, 550 F.3d at 454-55.

<sup>25</sup> *United States v. Sun Bank of Miami*, 609 F.2d 832, 833 (5th Cir. 1980).

<sup>26</sup> *LaBarge*, 550 F.3d at 455.

<sup>27</sup> LA. REV. STAT. ANN. §10:5-106 (2003).

<sup>28</sup> BROOKE WUNNICKE & DIANE WUNNICKE, *STANDBY LETTERS OF CREDIT* 100 (1989).

<sup>29</sup> KOZOLCHYK, *supra* note 12, at 83.

<sup>30</sup> *Id.* at 84.

<sup>31</sup> *Id.*

issue was subject to UCP400.<sup>32</sup> However, in order to properly understand the intent of the drafters of the UCP400 with regard to originality, one should consider prior and subsequent versions of the rules.

Prior to effectuation of the UCP400 in 1984, the UCP290<sup>33</sup> was the most current revision of the UCP having gone into effect in 1975. It addressed the issue of electronic transfer of a letter of credit in Article 4,<sup>34</sup> which stated that when an issuer uses cable, telegram, or telex to advise a letter of credit “and intends the mail confirmation to be the operative credit instrument, the cable, telegram or telex must state that the credit will only be effective on receipt” of the mail confirmation.<sup>35</sup> Article 4 further states that if the procedures of Article 4(a) are not followed, the issuer will be held responsible.<sup>36</sup> Section (c) of Article 4 elaborates further on the procedure to be followed when utilizing a cable, telegram, or telex, by stating that if the phrase “details to follow” (or similar wording) is not in the transmission, the issuer need not send a mail confirmation.<sup>37</sup> The general purpose of Article 4 was to take advantage of technological advances in communications between banks.<sup>38</sup> A shift had occurred in the banking community, and mailed instruments had been replaced by telecommunications for reasons of both timeliness and cost.

Finding the need to revise the rules in the banking community, the ICC Banking Commission, in 1983, laid out the UCP400<sup>39</sup>. The previous

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<sup>32</sup> *LaBarge*, 550 F.3d at 447.

<sup>33</sup> International Chamber of Commerce, *The Uniform Customs and Practice for Documentary Credits (UCP290)*, ICC Publication No. 290 (1974).

<sup>34</sup> UCP290, *supra* note 33, art. 4. In full, it states “(a) When an issuing bank instructs a bank by cable, telegram or telex to advise a credit, and intends the mail confirmation to be the operative credit instrument, the cable, telegram or telex must state that the credit will only be effective on receipt of such mail confirmation. In this event, the issuing bank must send the operative credit instrument (mail confirmation) and any subsequent amendments to the credit to the beneficiary through the advising bank. (b) The issuing bank will be responsible for any consequences arising from its failure to follow the procedure set out in the preceding paragraph. (c) Unless a cable, telegram or telex states “details to follow” (or words of similar effect), or states that the mail confirmation is to be the operative credit instrument, the cable, telegram or telex will be deemed to be the operative credit instrument and the issuing bank need not send the mail confirmation to the advising bank.”

<sup>35</sup> *Id.*

<sup>36</sup> *Id.*

<sup>37</sup> *Id.*

<sup>38</sup> H.C. GUTTERIDGE & MAURICE MEGRAH, *THE LAW OF BANKERS’ COMMERCIAL CREDITS* 14-15 (1984).

<sup>39</sup> UCP400, *supra* note 23.

Article 4 of UCP290 became Article 12<sup>40</sup> but with some alteration. Some changes were of little significance, such as the changing of “cable, telegram or telex” in UCP290 to the term “teletransmission” in UCP400 – the drafters merely intended to capture the rapid development of technology and communications devices.<sup>41</sup> However, of notable significance is the changing of wording from UCP290 Article 4(c) to UCP400 Article 12(b) regarding the sending of mail confirmation of a letter of credit.<sup>42</sup> The drafters of UCP290 utilized the phrase “need not,” leaving the provision open to broader interpretations.<sup>43</sup> When drafting UCP400, however, the language was strengthened to state, “no mail confirmation should be sent” unless the transmission contains some language to the effect that a mail confirmation would be sent.<sup>44</sup> UCP400 Article 12 creates a default rule that issuers must make it clear whether a teletransmission itself or a follow-up letter is the “operative credit instrument.”<sup>45</sup> Unless the teletransmission recites “full details to follow” (or something similar), the teletransmission is the credit instrument, and any attempt to add or subtract terms in a follow-up letter would be an ineffective attempt to amend the credit unilaterally.<sup>46</sup> The UCP400 continued to place the burden of responsibility on the issuer if these procedures were not followed.<sup>47</sup>

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<sup>40</sup> UCP400, *supra* note 23, art. 12. In full, UCP400 Article 12 states “(a) When an issuing bank instructs a bank (advising bank) by any teletransmission to advise a creditor an amendment to a credit, and intends the mail confirmation to be the operative credit instrument, or the operative amendment, the teletransmission must state “full details to follow” (or words of similar effect), or that the mail confirmation will be the operative credit instrument or the operative amendment. The issuing bank must forward the operative credit instrument or the operative amendment to such advising bank without delay. (b) The teletransmission will be deemed to be the operative credit instrument or the operative amendment, and no mail confirmation should be sent, unless the teletransmission states “full details to follow” (or words of similar effect), or states that the mail confirmation is to be the operative credit instrument or the operative amendment. (c) A teletransmission intended by the issuing bank to be the operative credit instrument should clearly indicate that the credit is issued subject to Uniform Customs and Practice for Documentary Credits, 1983 revision, ICC Publication 400. (d) If a bank uses the services of another bank or banks (the advising bank) to have the credit advised to the beneficiary, it must also use the services of the same bank(s) for advising any amendments. (e) Banks shall be responsible for any consequences arising from their failure to follow the procedures set out in the preceding paragraphs.”

<sup>41</sup> WUNNICKE & WUNNICKE, *supra* note 28; BERNARD WHEBLE, DOCUMENTARY CREDITS: UCP 1974/1983 REVISIONS, COMPARED AND EXPLAINED 26 (1984).

<sup>42</sup> UCP400 Article 12 (1983).

<sup>43</sup> *Id.*

<sup>44</sup> *Id.*

<sup>45</sup> *Id.*

<sup>46</sup> CHARLES MOONEY, JR., LETTERS OF CREDIT AND BANKERS’ ACCEPTANCES 69 (1985).

<sup>47</sup> UCP400, *supra* note 23, art. 12.



One element lacking in UCP290, however, was a better explanation of the term *original*, and the Banking Commission sought to rectify this with Article 22 of UCP400.<sup>48</sup> Article 22(c) states, “Unless otherwise stipulated in the credit, banks will accept as originals documents produced or appearing to have been produced: by reprographic systems; by, or as the result of, automated or computerized systems; as carbon copies, if marked as originals, always provided that, where necessary, such documents appear to have been authenticated.”<sup>49</sup> The article seems to stipulate that when documents are photocopied, the documents must be marked as an original, *on* the original writing itself, and not merely the word “original” photocopied onto it.<sup>50</sup>

Due to misinterpretations by the English courts in both *Glencore International AG v. Bank of China*<sup>51</sup> and *Kredietbank v. Midland Bank PLC*,<sup>52</sup> the ICC adopted UCP500<sup>53</sup> in 1994, in which changes were made to both prior Article 12 and 22 of UCP400. The drafters took their intentions from UCP400 Article 12, and made them even clearer with the language of UCP500 Article 11(a).<sup>54</sup> Going beyond merely telling issuing banks that they should not send mail confirmations when a teletransmission is the operative instrument, the drafters reiterate that the mail confirmation would have “no effect” and that the advising bank need not compare the mailed credit with the teletransmitted credit.<sup>55</sup> Furthermore, the text creates the

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<sup>48</sup> Adam Johnson, *Letters of Credit and Original Documents-Again*, 14 J.I.B.L. 287 (1999), reprinted in 2000 Annual Survey of Letter of Credit Law & Practice 116 (2000).

<sup>49</sup> UCP400, *supra* note 23, art. 22.

<sup>50</sup> RAYMOND JACK, DOCUMENTARY CREDITS 153 (1991) (stating that it would be “pointless if it were sufficient that a document which was a photocopy included the word ‘original’ photocopied onto it”). Although one wonders how an issuer would necessarily see this upon merely a facial examination of the documents.

<sup>51</sup> *Glencore Int'l AG v. Bank of China*, [1996] 5 Bank L.R. 1, 1 Lloyd's Rep. 135 (CA).

<sup>52</sup> *Kredietbank v. Midland Bank PLC*, [1999] 1 All E.R. (Comm.) 801 (A.C.).

<sup>53</sup> International Chamber of Commerce, *The Uniform Customs and Practice for Documentary Credits (UCP500)*, ICC Publication No. 500 (Jan. 1, 1994) [hereinafter UCP500].

<sup>54</sup> UCP500, *supra* note 53, art. 11. In full Article 11 states: “When an Issuing Bank instructs an Advising Bank by an authenticated teletransmission to advise a Credit or an amendment to a Credit, the teletransmission will be deemed to be the operative Credit instrument or the operative amendment, and no mail confirmation should be sent. Should a mail confirmation nevertheless be sent, it will have no effect and the Advising Bank will have no obligation to check such mail confirmation against the operative Credit instrument or the operative amendment received by teletransmission.”

<sup>55</sup> UCP500, *supra* note 53, art. 11.

presumption that the telecommunication is the only communication necessary when the teletransmission is authenticated.<sup>56</sup>

Concern in the banking community over the limited scope of UCP400 Article 22(c) caused the ICC to amend the language in UCP500 Article 20(b) to include more than just “reprographic, automated, or computerized systems.”<sup>57</sup> The provision can be read to require that “any documentation created by reprographic means, which would include a computer, must bear a stamp as an original.”<sup>58</sup> Although possible in theory, this result is neither reasonable nor consistent with practice.<sup>59</sup> Unfortunately, the imprecise draftsmanship led to misinterpretation in the courts.<sup>60</sup>

The final transformation of the electronic communication rule came in 2006 with the creation of the UCP600<sup>61</sup>. Article 11(a) states:

An authenticated teletransmission of a credit or amendment will be deemed to be the operative credit or amendment, and any subsequent mail confirmation shall be disregarded. If a teletransmission states “full details to follow” (or words of similar effect), or states that the mail confirmation is to be the operative credit or amendment, then the teletransmission will not be deemed to be the operative credit or amendment. The issuing bank must then issue the operative credit or amendment without delay in terms not inconsistent with the teletransmission.<sup>62</sup>

The Official Commentary of the ICC reinforces that 11(a) states a “more definitive rule that an authenticated teletransmission will be deemed to be

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<sup>56</sup> Based on a plain reading of UCP500, *supra* note 53, art. 11.

<sup>57</sup> International Chamber of Commerce, *UCP 500 & 400 Compared*, at 59, ICC Publication No. 511 (1993).

<sup>58</sup> James Byrne, *Ten Major Stages in the Evolution of LC Practice*, in 2004 ANNUAL SURVEY OF LETTER OF CREDIT LAW & PRACTICE 24 (2004).

<sup>59</sup> *Id.*

<sup>60</sup> See *Glencore Int'l AG v. Bank of China*, [1996] 5 Bank L.R. 1, 1 Lloyd's Rep. 135 (CA); *Kredietbank v. Midland Bank PLC*, [1999] 1 All E.R. (Comm.) 801 (A.C.).

<sup>61</sup> International Chamber of Commerce, *The Uniform Customs and Practice for Documentary Credits (UCP600)*, ICC Publication No. 600 (July 1, 2007) [hereinafter UCP600].

<sup>62</sup> UCP600, *supra* note 61, art. 11.

the operative documentary credit or amendment, and should mail confirmation be sent, it will be disregarded.”<sup>63</sup> Furthermore, the Commentary states that if an issuing bank were to intend the transmitted document not to be the operative instrument, then wording such as “full details to follow” or something similar must be used.<sup>64</sup>

The 2006 revision of the UCP also saw an entire article devoted to *originals*. The creation of the originals article was due to two factors. The first was the ever increasingly advancement of electronic transmission of documents.<sup>65</sup> The second was the court decisions in *Glencore* and subsequent cases that were based upon an interpretation of UCP500 Article 20(b) that was not in accordance with standard banking practice. Sub-Article 17(a) sets forth that “At least one original of each document stipulated in the credit must be presented.”<sup>66</sup> Sub-Articles 17(b) and (c) share some overlap in dealing with what will be accepted as an original. Sub-Article 17(b) states that an issuer shall treat any document bearing an apparently original signature, mark, stamp, or label of the issuer of the document, unless the document itself states otherwise.<sup>67</sup> Sub-Article 17(c) states that “unless a document indicates otherwise, a bank will also accept a document as original if it: appears to be written, typed, perforated or stamped by the document issuer’s hand; or appears to be on the document issuer’s original stationery; or states that it is original, unless the statement appears not to apply to the document presented.”<sup>68</sup>

### C. Statement of the Case

In order to pay for the purchase of 3,800 feet of thirty-inch steel pipe from LaBarge Pipe & Steel, Co. (“LaBarge”), PVF USA, LLC (“PVF”), had First Bank issue a standby letter of credit for US\$144,000 to secure payment to LaBarge in case of default.<sup>69</sup> After employees of LaBarge and First Bank met and finalized the letter of credit (the standby), a First Bank employee sent a facsimile message to LaBarge.<sup>70</sup> The cover sheet in the facsimile “stated: ‘Here is the letter of credit you requested. Please let me

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<sup>63</sup> International Chamber of Commerce, *Commentary on UCP 600*, at 51, ICC Publication No. 680 (Nov. 15, 2007).

<sup>64</sup> *Id.*

<sup>65</sup> JAMES E. BYRNE, *THE COMPARISON OF UCP600 & UCP500* 154-155 (2007).

<sup>66</sup> UCP600, *supra* note 61, art. 17.

<sup>67</sup> *Id.*

<sup>68</sup> *Id.*

<sup>69</sup> *LaBarge*, 550 F.3d at 446.

<sup>70</sup> *Id.*

know if you need any additional information.”<sup>71</sup> Upon receipt of the facsimile message, the LaBarge employee requested that First Bank amend the language of the standby.<sup>72</sup> After making the change, the First Bank employee sent a facsimile of the standby with the requested changes, this time with a cover sheet stating, “Here is the revision to the letter of credit you requested. Please let me know if you need any additional information.”<sup>73</sup>

The versions of the standby that the First Bank employee had originally transmitted to LaBarge via facsimile were claimed to have been kept by the employee.<sup>74</sup> The First Bank employee testified that a representative of PVC took the standby in early December.<sup>75</sup> However, the employee of PVC denied ever having received the letter of credit.<sup>76</sup> First Bank then informed LaBarge that the standby had been given to PVC.<sup>77</sup>

In January and February, LaBarge representatives talked on two occasions with First Bank employees about the documents necessary to present to First Bank in order to draw on the standby.<sup>78</sup> The LaBarge representatives informed First Bank that they were having trouble locating the original standby, to which First Bank responded that they would not honor a presentation which did not include the original standby.<sup>79</sup>

When LaBarge presented documents in February, in addition to the other required documents, it included both the facsimile-transferred versions of the standby that it had received and an “Affidavit of Beneficiary of Irrevocable Letter of Credit and Indemnification of Issuer signed by Michael Brand, CFO, Secretary, and Treasurer of LaBarge,” stating that, “the ‘original letter of credit’ could not be produced because it was not delivered to LaBarge and was lost or destroyed.”<sup>80</sup> The affidavit also stated that LaBarge would reimburse First Bank if another party were to present the original standby and successfully draw on the standby.<sup>81</sup>

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<sup>71</sup> *Id.*

<sup>72</sup> *Id.*

<sup>73</sup> *Id.*

<sup>74</sup> *Id.* at 447.

<sup>75</sup> *Id.*

<sup>76</sup> *Id.*

<sup>77</sup> *Id.* at 448.

<sup>78</sup> *Id.*

<sup>79</sup> *Id.*

<sup>80</sup> *Id.*

<sup>81</sup> *Id.*

First Bank dishonored this presentation, and LaBarge sued First Bank in the United States District Court for the Middle District of Louisiana, asserting claims of wrongful dishonor, breach of the standby, detrimental reliance, and breach of a good faith obligation.<sup>82</sup> The district court entered summary judgment for First Bank, and LaBarge appealed.<sup>83</sup>

The Fifth Circuit Court of Appeals ruled that the documents presented did not meet the requirements of strict compliance, because LaBarge presented the facsimile copy of the standby, while the standby required that “the original Irrevocable Letter of Credit must be presented with any drawing so that drawings can be endorsed on the reverse thereof.”<sup>84</sup> Determining that UCP400 Article 22 was not indicative of the meaning of an “original” document, the Fifth Circuit decided that the “plain meaning” of the term would govern.<sup>85</sup> Using *Black’s Law Dictionary*, the court determined that the term “original” meant “first copy or archetype; that from which another instrument is transcribed, copied, or imitated.”<sup>86</sup> Since the document presented was not the “original,” the presentation did not strictly comply.<sup>87</sup>

#### D. Important Cases

##### 1. *Glencore International AG v. Bank of China*<sup>88</sup> and *Kredietbank v. Midland Bank PLC*<sup>89</sup>

In *Glencore*,<sup>90</sup> the Bank of China refused to honor a presentation on a letter of credit in part because the beneficiary’s certificates lacked markings that indicated that they were “original.”<sup>91</sup> Among the documents to be presented to the issuer was a beneficiary’s certificate, which when created was photocopied onto identical paper for record keeping purposes.<sup>92</sup> When presentation occurred, beneficiary presented one of the photocopies

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<sup>82</sup> *Id.* at 448.

<sup>83</sup> *Id.*

<sup>84</sup> *Id.* at 455.

<sup>85</sup> *Id.* at 452.

<sup>86</sup> *Id.* at 452 (citing BLACK’S LAW DICTIONARY, 1099 (6th ed. 1990)).

<sup>87</sup> *Id.* at 455.

<sup>88</sup> *Glencore Int’l AG v. Bank of China*, [1996] 1 Lloyd’s Rep. 135 (CA).

<sup>89</sup> *Kredietbank v. Midland Bank PLC*, [1999] 1 All E.R. (Comm.) 801 (A.C.).

<sup>90</sup> *Glencore*, [1996] 1 Lloyd’s Rep. at 135.

<sup>91</sup> *Id.*

<sup>92</sup> *Glencore*, [1996] 1 Lloyd’s Rep. at 147.

bearing a blue ink signature, while none of the other documents (including the original print) were signed.<sup>93</sup> The Court of Appeal, Civil Division, stated that in the absence of stipulations in the credit to the contrary, the basic rule was that originals of all the documents are required.<sup>94</sup> The court then ruled that the documents were discrepant because they were not “marked as original.”<sup>95</sup>

Prior to the decision in *Glencore*, it was “understood that a document that appeared on its face to be an original did not have to be otherwise marked in order to indicate its originality.”<sup>96</sup> After the *Glencore* case, while some hoped for reform of the UCP’s provisions on originals, others suggested that until something was done that beneficiaries should “wield their rubber stamps and mark all documents ‘original’, except those which by the terms of the credit, are permitted to be copies.”<sup>97</sup> Despite the decision in *Glencore*, some experts believed that most courts would attempt to interpret UCP500 Article 20 in light of the international banking practices rather than the “plain language” approach of *Glencore*.<sup>98</sup>

In *Kredietbank*,<sup>99</sup> the letter of credit required the presentation of an original insurance policy, which was initially produced by printing a copy onto the insurance issuer’s watermarked, high-quality headed paper bearing the company’s blue logo and name. This printed document was then photocopied with the marking of “duplicate.” Both documents were signed by the insurance issuer and presented to the Issuer.<sup>100</sup>

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<sup>93</sup> *Id.*

<sup>94</sup> *Glencore*, [1996] 1 Lloyd’s Rep. at 147; Howard N. Bennett, *Strict Compliance Under U.C.P. 500*, [1997] 1 L.M.C.L.Q. 7.

<sup>95</sup> *Glencore*, [1996] 1 Lloyd’s Rep. at 147.

<sup>96</sup> James E. Byrne, *Editor’s Overview* to International Chamber of Commerce, *The Determination of an “Original” Document in the Context of UCP 500 Sub-Article 20(b)*, ICC Doc. No. 470/871 Rev. (July 12, 1999), in *LC RULES & LAWS CRITICAL TEXTS* 129 (James E. Byrne ed., 4th ed. 2007).

<sup>97</sup> Adam Johnson, *Letters of Credit and Original Documents-Again*, 14 J.I.B.L. 287 (1999), reprinted in 2000 Annual Survey of Letter of Credit Law & Practice 123 (2000) (citing Diana Wright, 10 J.I.B.L. Supplement (1995)).

<sup>98</sup> James Barnes, Opinion Letter by James G. Barnes on the Obligations of Issuing and Confirming Banks to Accept Documents as Originals (1999), reprinted in 1999 ANNUAL SURVEY OF LETTER OF CREDIT LAW & PRACTICE 306 (1999).

<sup>99</sup> *Kredietbank v. Midland Bank PLC*, [1999] 1 All E.R. (Comm.) 801 (A.C.).

<sup>100</sup> *Id.*

The Court of Appeal, Civil Division, stated that it was bound by the decision in *Glencore*<sup>101</sup>, to hold that Article 20(b) required an original to be “marked as original.”<sup>102</sup> However, the judge concluded that the document need not have the word “original” placed on it, but that the requirement was satisfied if the terms or markings on the document would leave “no doubt about it being the original.”<sup>103</sup> Finding that the printed insurance policy met this test because of the colored logo, the signatures, the terms of the document, and the existence of a document labeled as “duplicate,” the judge ruled that the document need not be marked as original.<sup>104</sup> Attempting to isolate the effect of *Glencore*, the judge stated that its holding “was not concerned with an original document which contained a relevant contract and which was not itself a copy of some other document and the judgment did not qualify the bank’s duty to accept a document of that kind as valid tender under a credit.”<sup>105</sup>

The decision in *Kredietbank* was a clear balk by the court to the holding in *Glencore*.<sup>106</sup> While hesitant to contradict the precedent set in *Glencore*, the judge nonetheless carved out a separate groove for the specific facts in *Kredietbank*.<sup>107</sup> This, however, failed to rectify the problem created by *Glencore*.<sup>108</sup> Fear still existed that the *Glencore* decision would continue to haunt the banking community, requiring formerly unnecessary (and in their mind still unnecessary) markings on originals to avoid dishonor.

## 2. ICC Determination of an Original

The holding in *Glencore* (and the less-than-total solution issued by *Kredietbank*) was met with significant confusion within the banking

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<sup>101</sup> *Glencore Int'l AG v. Bank of China*, [1996] 1 Lloyd's Rep. 135 (CA).

<sup>102</sup> *Kredietbank*, [1999] 1 All E.R. (Comm.) 809-12 (A.C.).

<sup>103</sup> *Id.*

<sup>104</sup> *Id.*

<sup>105</sup> H.C. GUTTERIDGE & MAURICE MEGRAH, *THE LAW OF BANKERS' COMMERCIAL CREDITS* 195 (Richard King ed., 8th ed. 2001) (1984).

<sup>106</sup> Adam Johnson, *Letters of Credit and Original Documents-Again*, 14 J.I.B.L. 287 (1999), reprinted in 2000 Annual Survey of Letter of Credit Law & Practice 119-120 (2000).

<sup>107</sup> Adam Johnson, *Letters of Credit and Original Documents-Again*, 14 J.I.B.L. 287 (1999), reprinted in 2000 Annual Survey of Letter of Credit Law & Practice 120 (2000).

<sup>108</sup> Adam Johnson, *Letters of Credit and Original Documents-Again*, 14 J.I.B.L. 287 (1999), reprinted in 2000 Annual Survey of Letter of Credit Law & Practice 119 (2000) (suggesting that the decision was neither sound in terms of legal theory or banking practice).

community.<sup>109</sup> Recognizing the need to clarify UCP500 Article 20(b), the ICC Commission on Banking Technique and Practice issued a decision stating the intended meaning of the sub-article (the Determination of an Original).<sup>110</sup> Supporting the approach taken in *Kredietbank*<sup>111</sup>, the Commission's decision simply restated the standard banking practices, including a direct contradiction of the *Glencore* holding.<sup>112</sup> The Commission's decision states that if a photocopied document is either "completed by the document issuer's hand marking" or if it is photocopied "onto original stationery," then the document constitutes an original.<sup>113</sup>

### 3. Subsequent Cases

The Commission's Determination was quickly applied in the American courts.<sup>114</sup> In *Voest-Alpine Trading USA Corp. v. Bank of China*, when the Bank of China declared that packing lists were discrepant when not stamped as original, Voest-Alpine Trading USA Corp., the beneficiary, brought a suit for wrongful dishonor.<sup>115</sup> The United States District Court for the Southern District of Texas,<sup>116</sup> referring to the ICC policy statement, ruled that these documents were considered original under UCP500 Article 20, because all of the documents had blue-ink signatures, and there was no requirement under UCP500 that the documents be marked as "original."<sup>117</sup>

In England, the courts still felt obligated to pay homage to *Glencore*, while doing everything in their power to evade its vortex. In *Credit Industrial et Commercial v. China Merchants Bank*<sup>118</sup>, the Queen's Bench Division, Commercial Court, differentiated the case from *Glencore*, because the documents were not known to be copies.<sup>119</sup> However, the court, in undertaking an analysis of the International Chamber of Commerce's policy

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<sup>109</sup> Byrne, *supra* note 96.

<sup>110</sup> International Chamber of Commerce, *The Determination of an "Original" Document in the Context of UCP 500 Sub-Article 20(b)*, ICC Doc. No. 470/871 Rev. (July 12, 1999) [hereinafter *The Determination of an Original*].

<sup>111</sup> GUTTERIDGE & MEGRAH, *supra* note 105, at 196.

<sup>112</sup> Byrne, *supra* note 96.

<sup>113</sup> *The Determination of an Original*, *supra* note 110.

<sup>114</sup> Byrne, *supra* note 96.

<sup>115</sup> *Voest-Alpine Trading USA Corp. v. Bank of China*, 167 F. Supp. 2d 940, 948, *aff'd*, 288 F.3d 262 (5th Cir. 2002) (S.D. Tex. 2000).

<sup>116</sup> Worth note, is that this is the same circuit that decided *LaBarge*.

<sup>117</sup> *Voest-Alpine*, 167 F. Supp. 2d at 948.

<sup>118</sup> *Credit Indus. et Commercial v. China Merchs. Bank*, [2002] EWHC (Comm) 973, [2002] 2 All E.R. 427 (Comm).

<sup>119</sup> *Id.*



statement, determined that if the statement applied to the facts of the case, then the documents complied as “original.”<sup>120</sup> Despite the issuers’ protests to the contrary, the court ruled that since the “UCP is a code produced and published by the ICC . . . [i]t [was] entirely legitimate for the ICC to seek to resolve any ambiguities in, or difficulties of interpretation of, the code.”<sup>121</sup> The court’s parting from *Glencore* was not lost on the banking community, which saw through the “polite forms of English judicial decisions” to see the hidden rebuke of the *Glencore* decision.<sup>122</sup>

Nearly 9,000 kilometers away in the Republic of Korea, the courts reached similar outcomes to those in *Credit Industrial* and *Voest-Alpine*. In *Sungsan Yanghaeng v. Bank of China*<sup>123</sup>, the Bank of China challenged documents that were produced by “reprographic or computerized systems” that did not bear an “original mark.”<sup>124</sup> The Seoul Court of Appeal of the Republic of Korea ruled that under the UCP500 (which the letter of credit was subject to), when “the documents bear the signature by the stamps or of the one’s own handwriting, it would be just to treat them as original not as copies produced by reprographic system etc.,” and, as such, the documents need not bear a marking of “original.”<sup>125</sup> Again in *Korea First Bank v. Korean Export Insurance Corp.*,<sup>126</sup> the court held that the mark of “original” need not be present when a signature of the beneficiary was present.<sup>127</sup>

## II. Analysis of *LaBarge* Decision

The Fifth Circuit’s decision in *LaBarge* on the originality issue that confronted it was inconsistent with the intent of the UCP, failed to consider the ambiguity inherent in the transmittal of the letter of credit, and did not properly consider case law regarding a facsimile as an original. To avoid confusion on the issue of what does constitute an original letter of credit, there are additional steps that could be taken, such as revising the UCP

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<sup>120</sup> *Id.*

<sup>121</sup> *Id.*

<sup>122</sup> James E. Byrne, *Commentary on Credit Industriel et Commercial v. China Merchants Bank*, [2002] EWHC (Comm) 973, [2002] 2 All E.R. 427 (Comm), in 2003 ANNUAL SURVEY OF LETTER OF CREDIT LAW & PRACTICE 180 (2003).

<sup>123</sup> Seoul Court of Appeal 12th Div., August 14, 1999, *Sungsan Yanghaeng v. Bank of China*, Case No. 98 na 18072 (R.O. Korea).

<sup>124</sup> *Id.*

<sup>125</sup> *Id.*

<sup>126</sup> Supreme Court 3rd Div., 2002, *Korea First Bank v. Korean Exp. Ins. Corp.*, Case No. 2000 da 63691 (R.O. Korea).

<sup>127</sup> *Id.*

provisions to more closely mirror those ISP Rule 4.15<sup>128</sup>, differentiating between *original* and *operative* in the text of the UCP, and broadening the language of the UCP to include letters of credit in its article dedicated to originals.

#### A. Inconsistent with Intention of ICC/ Text of UCP 400

The decisions by both the trial court and appellate court in *LaBarge* were inconsistent with the International Chamber of Commerce's intention in drafting the Uniform Customs and Practice for Documentary Credits. The Fifth Circuit acknowledged that the letter of credit presented was subject to UCP400 Article 12, but dismissed it as being contradictory to Article 22, which the Fifth Circuit deemed to apply only to "supporting documents."<sup>129</sup> The court reasoned that although Article 12 stated that a facsimile transmission of a letter of credit could act as the "operative" document, the terms "operative" and "original" might not be synonymous.<sup>130</sup> The court, looking to *Black's Law Dictionary* rather than banking practice, determined that "original" meant "the first copy or archetype; that from which another instrument is transcribed, copied or imitated."<sup>131</sup> Based on this definition of "original" the court concluded that the facsimile-transmitted letter of credit was not an original document.<sup>132</sup> Incredibly, the Fifth Circuit, referring to Louisiana statutory provisions,<sup>133</sup> determined that letters of credit could indeed be issued by facsimile, but only if they were "marked by the relevant bank as 'original'."<sup>134</sup> This limiting statement flew in the face of the ICC's Determination of Original Documents, which states several ways documents can be original without expressly marking documents as "original."<sup>135</sup>

Starting first with the expansion to include all teletransmissions in UCP400, Article 12 clearly indicates the status of the letter of credit. First Bank failed to state anything similar to "full details to follow," as required by UCP400 Article 12(a) to make a mail confirmation the operative instrument.<sup>136</sup> First Bank in fact took positive steps to state that the

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<sup>128</sup> International Chamber of Commerce, *The International Standby Practices (ISP98)*, rule 4.15, ICC Publication No. 590 (Jan. 1, 1999) [hereinafter ISP98].

<sup>129</sup> *LaBarge*, 550 F.3d at 542 n.8.

<sup>130</sup> *Id.* at 452-53.

<sup>131</sup> *Id.* at 452 (quoting BLACK'S LAW DICTIONARY 1099 (6th ed. 1990)).

<sup>132</sup> *Id.* at 453.

<sup>133</sup> LA. REV. STAT. ANN. §10:5-104 (2003).

<sup>134</sup> *LaBarge*, 550 F.3d at 451.

<sup>135</sup> The Determination of an Original, *supra* note 109.

<sup>136</sup> UCP400, *supra* note 23, art. 12.

facsimile was “the” letter of credit (although the ambiguity of this statement is addressed below).<sup>137</sup> Furthermore, under 12(b), since there was an absence of the phrase “full details to follow,” the UCP decreed that “no mail confirmation should be sent.”<sup>138</sup>

Although unnecessary, it would have been more prudent for the Fifth Circuit to have looked to subsequent publications of the UCP for the intent of the drafters or customs of banking practice, rather than rely on a dictionary. The same analysis would apply under UCP500 Article 11 (Teletransmitted and Pre-Advised Credits)<sup>139</sup> as it did under UCP400 Article 12, but with the added caveat that if First Bank had sent a mail confirmation, LaBarge would have been inclined to disregard the mailed letter of credit altogether.

Subsequent to the publication of the ICC’s Determination of an Original, courts should be inclined to look at the transmission at face value and determine if the document would be considered to be an original, rather than narrowly looking for the document to be “marked original.”<sup>140</sup> In contrast to the intent manifested in the ICC’s publications, the Fifth Circuit undertook no such analysis.

### **B. Inconsistent with the Use of Ambiguity in Banking Practice**

Under standard banking practice, when ambiguity exists in a letter of credit, it is to be construed against the drafter<sup>141</sup> or, more generally, the issuer.<sup>142</sup> The Fifth Circuit adopted this position in *United States v. Sun Bank of Miami*.<sup>143</sup> In *LaBarge*, the letter of credit was transmitted with a cover letter stating, “Here is the letter of credit you requested,” and a subsequent revision of the letter of credit with a cover sheet stating, “Here

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<sup>137</sup> *LaBarge*, 550 F.3d at 451.

<sup>138</sup> UCP400, *supra* note 23, art. 12.

<sup>139</sup> UCP500, *supra* note 53, art. 11.

<sup>140</sup> The Determination of an Original, *supra* note 110.

<sup>141</sup> *Bath Iron Works Corp. v. WestLB*, 2004 U.S. Dist. LEXIS 6212, at \*9 (S.D.N.Y., Sept. 8, 2004) (citing *Barclay Knitwear Co., Inc. v. King’swear Enter. Ltd.*, 533 N.Y.S.2d 724 (1st Dep’t 1988)).

<sup>142</sup> *3Com Corp. v. Banco Do Brasil, S.A.*, 2 F. Supp. 2d 452 (S.D.N.Y. 1998), *aff’d*, 171 F.3d 739 (2d Cir. 1999) (granting the beneficiary’s motion for summary judgment when issuer failed to provide the “clear and unequivocal” notice required to terminate the LC by the UCP and New York law, holding that ambiguities in the LC should be construed against the drafter, in this case the issuer).

<sup>143</sup> *United States v. Sun Bank of Miami*, 609 F.2d 832, 833 (5th Cir. 1980). (holding that the though the issuer might have intended to limit use of funds for specified purposes, it failed to require such in documentation).

is the revision to the letter of credit you requested.”<sup>144</sup> A plain reading of these terms would suggest that the accompanying letter of credit was *the* letter of credit. However, since the same phrases could be read (as the court did) to mean that the facsimile is a copy of the original credit, there are at least two interpretations associated with the transmission. Under standard banking practice, because ambiguities associated with the letter of credit are to be held against the drafter, the facsimile-sent letters of credit were the originals. The court, in failing to recognize valid ambiguities, was precluded from this outcome.

### C. Inconsistent with prior decisions in the US and Internationally

In light of the British courts’ reluctance<sup>145</sup> to overturn *Glencore*, it would be possible to decide that since the facsimile-transmitted credits from First Bank were not marked as an original (i.e. had the word *original* or something similar emblazoned upon the letter of credits themselves), they were not originals under the meaning of UCP400 Article 22(b)<sup>146</sup> (the predecessor of UCP500 Article 20(b)<sup>147</sup>). On its face it would appear that the exception carved out by the Court of Appeal in *Kredietbank* would not necessarily apply to the facts presented to the Fifth Circuit either. Unlike the facsimile-transmitted documents sent to LaBarge, the documents in *Kredietbank* left no doubt in the court’s mind that they were original because of the colored logo, signatures, terms of the document, and the existence of a document marked “duplicate.”<sup>148</sup> However, despite the dissimilarity of the precise facts, the Fifth Circuit could have reached a

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<sup>144</sup> *LaBarge*, 550 F.3d at 453.

<sup>145</sup> It is worth noting, that generally, English courts have a different, more strict, notion of precedence than their U.S. counterparts. Even dicta can be binding. See Raj Bhala, *Symposium: Global Trade Issues in the New Millennium: The Power of the Past: Towards De Jure Stare Decisis in WTO Adjudication*, 33 *Geo. Wash. Int'l L. Rev.* 873, 888 (2001) (citing ALEXIS DE TOCQUEVILLE, *DEMOCRACY IN AMERICA* 267-68 (J.P. Mayer ed., George Lawrence trans., Yale Univ. Press 1969) (1850)) (“The English lawyer values laws not because they are good but because they are old; and if he is reduced to modifying them in some respect, to adapt them to the changes which time brings to any society, he has recourse to the most incredible subtleties in order to persuade himself that in adding something to the work of his fathers he has only developed their thought and completed their work. Do not hope to make him recognize that he is an innovator; he will be prepared to go to absurd lengths rather than to admit himself guilty of so great a crime. It is in England that this legal spirit was born, which seems indifferent to the substance of things, paying attention only to the letter, and which would rather part company with reason and humanity than with the law.”).

<sup>146</sup> UCP400, *supra* note 23, art. 22.

<sup>147</sup> UCP500, *supra* note 53, art. 20.

<sup>148</sup> *Kredietbank v. Midland Bank PLC*, [1999] 1 All E.R. (Comm.) 807-12 (A.C.).

similar result as *Kredietbank*'s, if it had found the language of the cover sheets to be indicative that the transmitted documents were the original letters of credit.<sup>149</sup>

Although the Fifth Circuit's analysis of the originality of the documents appears to be in line with the *Glencore* and *Kredietbank* decisions, the cases after the ICC Determination of an Original presented an opportunity for the court to analyze the documents for originality despite the lack of an express marking of the word *original*. The decision in *Voest-Alpine* stood for greater acceptability under the interpretation of the UCP under the ICC Determination of an Original under Article 20 of UCP500.<sup>150</sup> The decisions of international courts are consistent with the opinions of *Voest-Alpine* in that they accept as "original" reproduced or computerized versions of documents at presentation.<sup>151</sup> The Fifth Circuit failed to acknowledge these cases, which had shown precedent and practice to favor allowance of facsimile-reproduced materials as original documents, when they merely appeared on their face to be the original. The court failed to look at the presented documents as a bank unaware of the letters of credit's statuses would – which would be without presumption of the knowledge of the documents' facsimile origins. However, under the facts given to the Fifth Circuit, First Bank was not unaware of the origin of the documents presented to it.<sup>152</sup> First Bank was probably faced with an obvious ground for dishonor when the beneficiary indicated in the documents presented that the LC was not the original because the "original letter of credit" could not be produced because it was not delivered to LaBarge and was lost or destroyed."<sup>153</sup>

Despite having this isolated ground as a reason to find valid grounds for dishonor<sup>154</sup>, the Fifth Circuit based its holding on the "plain meaning" of the term "original," precluding nearly all facsimile-transmitted letters of credit unless marked "original."<sup>155</sup> This holding presents bankers with a

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<sup>149</sup> *LaBarge*, 550 F.3d at 446-47.

<sup>150</sup> *Voest-Alpine Trading USA Corp. v. Bank of China*, 167 F. Supp. 2d 940 (S.D. Tex. 2000), *aff'd*, 288 F.3d 262 (5th Cir. 2002).

<sup>151</sup> *Credit Indus. et Commercial v. China Merchs. Bank*, [2002] EWHC (Comm) 973, [2002] 2 All E.R. 427 (Comm); Seoul Court of Appeal 12th Div., August 14, 1999, *Sungsan Yanghaeng v. Bank of China*, Case No. 98 na 18072 (R.O. Korea); Supreme Court 3rd Div., 2002, *Korea First Bank v. Korean Exp. Ins. Corp.*, Case No. 2000 da 63691 (R.O. Korea).

<sup>152</sup> *LaBarge*, 550 F.3d at 448.

<sup>153</sup> *Id.*

<sup>154</sup> The issuer was aware that the standby present was not the original.

<sup>155</sup> *LaBarge*, 550 F.3d at 451-52 (5th Cir. 2008).

similar problem to the one created by *Glencore*. The Fifth Circuit in *LaBarge* essentially incorporated the *Glencore* holding to American jurisprudence because now, when transmitting letters of credit via facsimile, the letters must be marked as “original.”<sup>156</sup>

#### D. Possible Solutions

Although not a new idea<sup>157</sup>, one wonders if the International Banking Commission’s intention would not be better served if a clearer rule on originals was incorporated into the UCP. Rule 4.15 of the International (ISP98)<sup>158</sup> was intended to restate and clarify UCP500 Article 20 to better conform to standard banking practice.<sup>159</sup> Rule 4.15 provides:

- a. A presented document must be an original.
- b. Presentation of an electronic document record, where an electronic presentation is permitted or required, is deemed to be an “original”.
- c.
  - i. A presented document is deemed to be an original unless it appears on its face to have been reproduced from an original.
  - ii. A document which appears to have been reproduced from an original is deemed to be an original if the signature or authentication appears to be original.
  - ....
- d. If multiples of the same document are requested, only one must be an original<sup>160</sup>

The ISP98’s solution is attractive because it creates “a presumption that *all* documents presented are originals, unless they appear on their face to have been produced from some other document or documents.”<sup>161</sup> Furthermore, under sub-rule (c)(i), even if the letter of credit is reproduced from an

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<sup>156</sup> *LaBarge*, 550 F.3d at 451. The court failed to state any other situations when the facsimile copy would be accepted as the original, creating uncertainty in situations other than involve an express marking as an original.

<sup>157</sup> See Adam Johnson, *Letters of Credit and Original Documents-Again*, 14 J.I.B.L. 287 (1999), reprinted in 2000 Annual Survey of Letter of Credit Law & Practice 122-123 (2000).

<sup>158</sup> ISP98, *supra* note 128.

<sup>159</sup> JAMES E. BYRNE, THE OFFICIAL COMMENTARY ON THE INTERNATIONAL STANDBY PRACTICES 179 (James G. Barnes ed., 1999).

<sup>160</sup> ISP98, *supra* note 128.

<sup>161</sup> Adam Johnson, *Letters of Credit and Original Documents-Again*, 14 J.I.B.L. 287 (1999), reprinted in 2000 Annual Survey of Letter of Credit Law & Practice 118 (2000).

original, it would constitute an original if it bears an original signature.<sup>162</sup> Therefore, even if such wording (as is found in the ISP98) were incorporated into a UCP revision, the outcome of this case would have been the same; although, all that would have been necessary for LaBarge to do was to have signed the document (or mark it in some way).<sup>163</sup> This solution would certainly be an improvement over the outcome in *LaBarge*, in which the Fifth Circuit determined that facsimiles, unless marked as “original,” were not in compliance with the originality requirement.<sup>164</sup>

A second more tailored solution that could be undertaken by the ICC would be to include the word “original” in addition to “operative” in future adaptations of UCP600 Article 11. This would relieve possible confusion stemming from an increased reliance on electronic means of communication. Or, similarly, simply defining “operative” would help to alleviate confusion over the use of two separate terms in UCP400 Article 12 and 22.<sup>165</sup>

A third possible solution would be to broaden the scope of the text (if maybe not the intended scope) of future versions of UCP600 Article 17 (“Original Documents”). The Fifth Circuit in *LaBarge* determined that UCP400 Article 22 was not intended to apply to letters of credit, but only to their “supporting documents.”<sup>166</sup> With this precedent set, it would not be impossible to foresee a future decision limiting the scope of UCP600 Article 17 to “supporting documents.”<sup>167</sup> Therefore explicit language in future revisions of UCP600 Article 17 detailing its application to letters of credits as well as other supporting documents could alleviate the discrepancy between practice and court decisions such as *Glencore*.

However, the problem with the latter two solutions is that they would not affect letters of credit already in existence under UCP600 or earlier. This was the case when the ICC issued its Determination of an Original because it applied to UCP500, but not UCP400, and therefore, letters of credit issued under UCP400 almost seem immune to the attempted clarification of banking practice in court. However, if courts were forward-looking enough to recognize the intent of the ICC and read the prior version

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<sup>162</sup> JAMES E. BYRNE, THE OFFICIAL COMMENTARY ON THE INTERNATIONAL STANDBY PRACTICES 180 (James G. Barnes ed., 1999).

<sup>163</sup> *Id.*

<sup>164</sup> *LaBarge*, 550 F.3d at 451.

<sup>165</sup> *LaBarge*, 550 F.3d at 452-53.

<sup>166</sup> *LaBarge*, 550 F.3d at 452 n.8.

<sup>167</sup> *Id.*

of the UCP with an eye toward that intent, the solution could be partially viable.

### Conclusion

The United States Court of Appeals, Fifth Circuit, in deciding *LaBarge Pipe & Steel Co. v. First Bank*, erred in determining that the presentation was non-complying. Both the prior and subsequent versions of the Uniform Customs and Practice for Documentary Credits produced by the International Chamber of Commerce, which had been published by the time of the trial, indicated through their respective articles governing teletransmissions and originals, that the letter of credit issued via telefax by First Bank was, indeed, original.<sup>168</sup> In cohesion with the text of the UCP, the telefaxed letter of credit would not have been sufficient as the original if the cover page had indicated that “full details [were] to follow,” but this was not the case.<sup>169</sup> The holdings of both American and foreign courts support the sufficiency of electronically transmitted documents under the circumstances in *LaBarge*.<sup>170</sup> The court here disregarded such notions and, instead, held that the beneficiary, LaBarge, would have been required to submit a document that was neither sent to it, nor should have been expected to have been sent to it. Furthermore, the Fifth Circuit ignored the ambiguity present in the facsimile from First Bank.<sup>171</sup> If the court had acknowledged that the language used in the issuer’s cover sheet could have been interpreted to create an original document, such ambiguity would have to be read in favor of the beneficiary, LaBarge, under standard banking practices.<sup>172</sup>

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<sup>168</sup> UCP600, *supra* note 61, art. 11; UCP500, *supra* note 53, art. 12.

<sup>169</sup> UCP600, *supra* note 61, art. 11.

<sup>170</sup> See *Voest-Alpine Trading USA Corp. v. Bank of China*, 167 F. Supp. 2d 940 (S.D. Tex. 2000), *aff'd*, 288 F.3d 262 (5th Cir. 2002); *Sungsan Yanghaeng v. Bank of China*, 1998 NA 18072.; *Korea First Bank v. Korean Exp. Ins. Corp.*, 2000 DA 63691.

<sup>171</sup> *LaBarge*, 550 F.3d at 453.

<sup>172</sup> *United States v. Sun Bank of Miami*, 609 F.2d 832, 833 (5th Cir. 1980) (holding that though the issuer might have intended to limit use of funds for specified purposes, it failed to require such in documentation); see also *Bath Iron Works Corp. v. WestLB*, 2004 U.S. Dist. LEXIS 19206, at \*9 (S.D.N.Y., Sept. 8, 2004) (citing *Barclay Knitwear Co., Inc. v. King'swear Enter. Ltd.*, 533 N.Y.S.2d 724 (1st Dep't 1988)); *3Com Corp. v. Banco Do Brasil, S.A.*, 2 F. Supp. 2d 452 (S.D.N.Y. 1998), *aff'd*, 171 F.3d 739 (2nd Cir. 1999) (granting the beneficiary’s motion for summary judgment when issuer failed to provide the “clear and unequivocal” notice required to terminate the LC by the UCP and New York law, holding that ambiguities in the LC should be construed against the drafter, in this case the issuer).



The holding in *LaBarge* imposed a standard of analysis upon letter of credit issuance that was not only unintended by the ICC, but specifically guarded against with the UCP400 drafters' modification of Article 12. The most viable options appear to be either a court reversing or rebutting the *LaBarge* decision or a new ICC revision. The latter option, while leaving future parties using letters of credit subject to the UCP in a better position of knowing what the original document is, offers little consolation to LaBarge Pipe & Steel Co. for its US\$144,000 loss.