

Remedies for Breach of a Buyer's Obligation to Open a Letter of Credit in CISG Contracts—Part II

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A clause in a sales contract requiring the buyer to open a letter of credit creates an obligation for the buyer to have a bank assume an obligation to pay the contract price against documents towards the beneficiary of the credit, i.e. the seller. This obligation to open a letter of credit is enforceable under the law governing the sales contract. Questions arise as to the enforcement and effects of the buyer's obligation under that law. In particular, whether failing to open the letter of credit, or a non-compliant letter of credit, may entitle the seller to claim certain remedies but exclude others. The author submits that the United Nations Convention on the International Sale of Goods ("CISG") offers an effective legal framework for the enforcement of a buyer's obligation to have a bank opening a letter of credit under a contract for the international sale of goods. This article discusses the remedies that may follow from a buyer's breach of a contractual obligation to open a letter of credit pursuant to the CISG. The first part of the article, which appeared in the March 2017 issue of The Banking Law Journal, introduced the topic. This final part of the article analyzes the remedies that may follow from a buyer's breach of a contractual obligation to open a letter of credit pursuant to the CISG, discusses a buyer's right to suspend performance of a contractual obligation to open a letter of credit and other interdependent obligations, as well as a buyer's right to stop payment after opening of a letter of credit, and provides a reminder of the legal effect of the avoidance of the underlying contract over a letter of credit.

REMEDIES FOR BREACH OF A PARTY'S DUTY TO OPEN A (PROPER) LETTER OF CREDIT

The buyer's failure to perform any of his obligations will entitle the seller to claim the legal remedies available to him pursuant to Article 61 CISG.¹ A

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¹ LOOKOFSKY, 140. 2012; ALEJANDRO M. GARRO & ALBERTO L. ZUPPI, *COMPRVENTA INTERNA-*

breach will ensue regardless of whether the obligation at stake is a main obligation or an ancillary one, whether it arises under the CISG provisions or the sales contract.² A buyer's failure to have the agreed letter of credit opened by a bank constitutes a breach of contract.³ Accordingly, the seller may be entitled to some of the remedies afforded by the CISG. These remedies include a request for specific performance, the avoidance of the sales contract, and damages.

Right to Request Specific Performance of an Obligation to Provide a Letter of Credit

The CISG gives a party the remedy to require performance by the other party of its obligations, unless the former had opted for a different remedy that is inconsistent with specific performance, such as the avoidance of the sales contract.⁴ Possible breaches giving rise to the remedy of specific performance include the failure to pay the price, related documents or their defective delivery, and also other contractually accepted obligations,⁵ like the opening of a letter of credit by the buyer.⁶ In the case of a letter of credit which terms depart from agreed specifications, the seller may require the buyer to have a bank issuing a substitute letter of credit or to amend its nonconforming terms. A buyer may nevertheless be exempted from performing its obligation to open a letter of credit due to an impediment beyond its own or the bank's control and that was unforeseeable and unavoidable either by the buyer or the bank pursuant to Article 79(1)(2)(a)(b) CISG.⁷

CIONAL DE MERCADERÍAS 285 (AbeledoPerrot. 2012); JOHN O. HONNOLD, *UNIFORM LAW FOR INTERNATIONAL SALES* 377 (Kluwer Law International. 1999).

² LOOKOFSKY, 140. 2012.

³ Mohs, Article 61 898, 899. 2016; RAMBERG, 142. 2011; UNCITRAL, *DIGEST OF CASE LAW ON THE UNITED NATIONS CONVENTION ON CONTRACTS FOR THE INTERNATIONAL SALE OF GOODS* Comments on Art. 54 (United Nations Commission for International Trade Law. 2012).

⁴ Articles 61 and 62 CISG; HONNOLD, 378, 379. 1999; GARRO & ZUPPI, 287. 2012; LOOKOFSKY, 140, 141. 2012.

⁵ Art. 62 CISG.

⁶ LOOKOFSKY, 141. 2012; Shael Herman, *Specific Performance: a Comparative Analysis*, 7 *EDINBURGH LAW REVIEW* 5, 196 (2003).

⁷ CHRISTOPH BRUNNER, *FORCE MAJEURE AND HARDSHIP UNDER GENERAL CONTRACT PRINCIPLES: EXEMPTION FOR NON-PERFORMANCE IN INTERNATIONAL ARBITRATION* 187 § 18 (Kluwer Law International. 2008): "the obligor has basically no control over these third parties. Paragraph 2 thus only applies if the third party independently discharges a performance obligation of the obligor. Firstly, this is the case for transport companies or banks, inasmuch as they independently perform certain obligations of the seller or the buyer (e.g., to transport the goods, to transfer the money to the seller's bank, to open a letter of credit or to establish a bank guarantee)."

Fixing an Additional Period of Time to Open a Letter of Credit

For the sake of goodwill among the parties or for its own benefit, a seller may fix an additional period of time for performance by the buyer of any contractual or statutory obligations pursuant to Article 63 (1) CISG. The setting of an additional period of time also works for a contractual obligation to provide a conforming letter of credit.⁸ In the case of a buyer's breach of the obligation to pay the price, Article 63(1) CISG is of paramount importance because a repeated failure to pay the price within the additional period of time fixed by the seller will automatically entitle the seller to declare the avoidance of the contract pursuant to Article 64 (1)(b) CISG.⁹ A question arises as to whether the buyer's breach to have a bank issuing a letter of credit entitles the seller to avoid the contract on the grounds of 64 (1)(b) CISG or if the seller's right to avoid the contract depends only on the fundamental nature of the breach pursuant to Articles 25 and 64(1)(a) CISG. An answer to this question is offered below.

In all cases, the additional period of time fixed by the buyer must be of a reasonable length determined by the circumstances (Article 63(1) CISG) and the CISG's general policy against the avoidance of the contract on insubstantial grounds.¹⁰ In the context of an obligation to have a bank issuing a new or proper letter of credit, due regard must be had to the banking practices at the buyer's place of business, bank holidays, the type of letter of credit agreed upon and its payment structure, *i.e.* whether the letter of credit is a non-confirmed or confirmed one. In this line of thought, the issuance of "confirmed" letter of credit may need a longer additional period of time than a non-confirmed one because of the involvement of the confirming bank at the seller's place of business and the authorization required from the issuing bank. In relation to this, an ICC Tribunal found that an additional period of time of 20 days granted by the seller was reasonable, especially because some letters of credit can ordinarily be opened within few hours from their request.¹¹

⁸ Mohs, Article 63 914, 915. 2016: "article 63 is not restricted to any particular obligation of the buyer; the seller may set additional periods of time with respect to any of the buyer's obligations"; UNCITRAL, Comments Art. 63. 2012. *See also* Australia November 17, 2000 Supreme Court of Queensland, *Downs Investments v. Perwaja Steel*, available at <http://cisgw3.law.pace.edu/cases/001117a2.html>; China February 4, 2002 CIETAC Arbitration proceeding (Styrene monomer case) available at <http://cisgw3.law.pace.edu/cases/020204c1.html>; Switzerland February 20, 1997 District Court Saane (Spirits case) available at <http://cisgw3.law.pace.edu/cases/970220s1.html>.

⁹ Mohs, Article 63 915. 2016; UNCITRAL, Comments Art. 63(1). 2012.

¹⁰ HONNOLD, 385. 1999.

¹¹ ICC Arbitration Case No. 11849 of 2003 (Fashion products case) available at <http://>

The seller will be bound to hold any other remedy during the additional period of time unless the buyer informs that it does not intend to perform during such period (Article 63(2) CISG).¹²

Possibility to Request an Opportunity to Remedy a Nonconforming Letter of Credit

Pursuant to Article 48 CISG, the seller may request the buyer the opportunity to remedy a defective performance of its obligations, even after the due date of performance, if the seller can do so within unreasonable delay or without causing an unreasonable inconvenience or uncertainty to the buyer.¹³ There is no express corresponding buyer's right to remedy a defective performance of its obligation after the due date. However, this right constitutes a principle upon which the CISG is based (Article 7(2) CISG) and thus should be extended to the buyer. The right to remedy at one's own expenses exists for every type of breach of contract.¹⁴ It includes a violation of any agreed obligation like the provision of a letter of credit.

Article 48(1) CISG provides that the opportunity to remedy does not exist until after the due date of performance. Prior to the date of performance of the obligation to open a letter of credit, the curing of defects is also possible for the buyer if we apply by analogy Articles 34 and 37 CISG regarding early performance of the seller's obligations.¹⁵

The way a buyer is to remedy his failure ensues from the nature of the obligation breached. Accordingly, a defective letter of credit can be replaced by a new letter of credit.¹⁶ The precondition is always that the failure is of a nature that allows itself to be remedied. Whether the buyer is able to remedy its breach without "unreasonable delay," "unreasonable inconvenience," or "unreasonable uncertainty of reimbursement of expenses" for the seller cannot be decided as a general principle, but shall be answered only on the basis of the circumstances

cisgw3.law.pace.edu/cases/031849i1.html; also cited by LOOKOFSKY, 143. 2012.

¹² Mohs, Article 63 915. 2016.

¹³ LARRY DiMATTEO, *INTERNATIONAL CONTRACTING: LAW AND PRACTICE* 261 (Wolters Kluwer Third Edition ed. 2013); GARRO & ZUPPI, 216. 2012.

¹⁴ Markus Müller-Chen, *Article 48*, in SCHLECHTRIEM & SCHWENZER: *COMMENTARY ON THE UN CONVENTION ON THE INTERNATIONAL SALE OF GOODS* 764, 765, (Ingeborg Schwenzer ed. 2016).

¹⁵ BRIDGE, 284. 2013: referring to English case law in footnote 259 "it appears to be settled that, provide the buyer opens a confirming letter of credit by the due date, a non-conforming letter of credit may be cured by the bank's issue of an amending letter."

¹⁶ Müller-Chen, 765. 2016. Müller-Chen actually states that "a defective bank guarantee can be replaced by a new guarantee," but we consider that the example must apply by analogy to letters of credit.

of each individual case.¹⁷ In the case of an obligation to open a letter of credit, the buyer's steps to remedy its failure to comply in time may not often suit the seller. In particular if the seller has already acquired the right to avoid the contract because timely opening of the letter of credit was of the essence (see below). In other cases, consideration must be given to whether the opening of a new letter of credit, after its due date, causes the seller any unreasonable inconvenience or uncertainty. In this regard, a buyer may not always be entitled to remedy its failure to provide a proper letter of credit; applying Article 48(1)(2) CISG by analogy to the buyer.

Avoidance of the Underlying Contract Caused by Failure to Open a Letter of Credit as Agreed Upon by the Parties

Pursuant with Article 64(1) CISG, the seller may declare the sales contract avoided, to the extent the buyer's failure to perform any of its obligation amounts to a fundamental breach.¹⁸ In accordance with Article 25 CISG, a breach is fundamental if it results in such a detriment to the suffering party as to substantially deprive it of what it was entitled to expect under the contract, and such result was, or ought to be, foreseeable for the breaching party.¹⁹ The seller may also avoid the contract if the buyer does not, within the additional period of time fixed by the seller in accordance Article 63(1) CISG, perform its obligation to pay the price.

In relation to Article 63(1) CISG, some authors advocate that the failure to open a letter of credit is considered a breach of the buyer's obligations to pay the price under Articles 53 or 54 CISG²⁰ and, therefore, the seller may fix an additional period of time for the buyer to open the letter of credit agreed under the CISG contract, failing which the seller will be entitled to the remedy of avoidance.²¹ We consider that the opening of the letter of credit in time may not always equal to the obligation to pay the price. A letter of credit is not in

¹⁷ *Id.* at 765, 766.

¹⁸ LOOKOFKY, 142. 2012.

¹⁹ Article 25 CISG; Aneta Spaic, *Interpreting Fundamental Breach, in* INTERNATIONAL SALES LAW: A GLOBAL CHALLENGE 241, (Larry DiMatteo ed. 2014): "article 25 indicates that the criterion is not the degree of damage, but the importance of the underlying interest, the obligations under the contract, and the resulting consequences for the injured party."

²⁰ HONNOLD, 351, 352, 387. 1999. Mohs, Article 64 927. 2016. LOOKOFKY, 90. 2012: who mentions the ICC Arbitration Case No. 7197 of 1992 (*Failure to open letter of credit and penalty clause case*) available at <http://cisgw3.law.pace.edu/cases/927197i1.html>; as a breach of Article 54 CISG, failure to take the steps to perform payment, and awarded the remedy of damages.

²¹ Mohs, Article 64 927. 2016; HONNOLD, 351, 352, 384. 1999.

itself payment but contains a promise of payment.²² The buyer can ultimately neglect its obligation to open a letter of credit but still comply with its obligation to pay the price by other means, e.g. by cash wire transfer.²³ In that case, however, the buyer will take the risk of paying directly the price before the goods are shipped by the seller or the documents agreed under the letter of credit are handed over to the buyer. A well advised seller will not release the goods or the documents representing them until its bank account is credited with the price that was supposed to be covered by the initially agreed letter of credit. Otherwise, the question of whether the seller has a right to avoid the contract should depend on the objective importance of the buyer's breach to open a workable letter of credit in time.²⁴ Article 25 CISG will thus lead us to diverse solutions that are appropriate to individual cases.

Against this background, failure to open a workable letter of credit in time will most likely constitute a fundamental breach always. Whether we considered the obligation to open a letter of credit as a payment obligation under Article 53 or as merely as steps to perform payment under Article 54, delay could impair seller's main expectation under a sales contract.²⁵ For example, this can occur when the CISG contract stipulates that the seller has an immediate right to contract avoidance should the buyer fail to open the agreed letter of credit in time (Article 6 CISG).²⁶ In addition, the type of contract may make the opening of workable letter of credit in time being of the essence. For example, if the letter of credit is linked with the seller's duty to load the goods on the ship, its correct and timely opening is of the essence and the seller is entitled to avoid the contract for the slight delay or mistake in the letter of credit.²⁷

In a case that has been reported by some authors as an example of the rule that a CISG contract may be avoided due to the buyer's failure to open a letter of credit in time,²⁸ the Supreme Court of Queensland arrived to this conclusion

²² BRIDGE, 287. 2013.

²³ *Id.* at 295.

²⁴ RAMBERG, 152, 153. 2011.

²⁵ *But see* Mohs, Article 64 926. 2016: "the seller may not immediately avoid the contract. The reason for this position is that the letter of credit is usually given to secure the seller's performance. If the seller has not yet started shipping the goods, he has no exposure that would require coverage by an immediate right to avoid the contract."

²⁶ *Id.* at 927; Spaic, 244. 2014. The parties can also agree that the existence of the contract is subject to the condition of precedent of opening a letter of credit, *see* BRIDGE, 292. 2013.

²⁷ Mohs, Article 64 926. 2016; BRIDGE, 275. 2013: discussing several cases supporting this view under English law.

²⁸ LOOKOFKY, 142, fn. 306. 2012.

only because of the specific facts at stake. In particular, the payment clause in that case required the provision of the letter of credit prior to the commencement of loading of the shipment of scrap metal.²⁹ The buyer refused to open the letter of credit at a time when the cargo was standing by the port of shipment for commencement of loading the scrap steel so that it might complete its loading program before the buyer could open the letter of credit in the time required by the contract.³⁰ In a case decided by a CIETAC arbitral tribunal, the circumstances were similar.³¹ The buyer was required to open the letter of credit days before the seller organizes the loading of goods under a CFR Incoterms. As per the buyer's request, the seller granted an additional period of time to open the letter of credit, but the buyer failed again. The arbitral Tribunal upheld the seller's right to avoid the contract in consideration of the CFR Incoterms, the additional period of time and the perishable nature of the goods at stake.³² In a different case decided by a Swiss court, the remedy of contract avoidance was granted after two grace periods to open the letter of credit that had to be opened prior to the seller obligation to ship the goods under a CIF Incoterms.³³ On the contrary, Austria Supreme Court decided that the seller was not entitled to avoid the contract for the buyer's breach to open a letter of credit in time because under the FOB Incoterms and the contract itself, the seller had to inform first the buyer about the port of loading and he had failed to do so in time.³⁴

Where time is not of the essence (because the letter of credit is not linked with the seller's duty to load the goods on the ship or otherwise), a question arises as to whether it may be concluded from the failure to open a letter of credit that the buyer will not perform the obligation to pay the price.³⁵ For example, if buyer is to make a deferred payment³⁶ through a letter of credit to

²⁹ Australia November 17, 2000 Supreme Court of Queensland, *Downs Investments v. Perwaja Steel*, available at <http://cisgw3.law.pace.edu/cases/001117a2.html>.

³⁰ *Ibid.*

³¹ China February 4, 2002 CIETAC Arbitration proceeding (Styrene monomer case) available at <http://cisgw3.law.pace.edu/cases/020204c1.html>.

³² *Ibid.*

³³ Switzerland February 20, 1997 District Court Saane (Spirits case) available at <http://cisgw3.law.pace.edu/cases/970220s1.html>.

³⁴ Austria February 6, 1996 Supreme Court (Propane case) available at <http://cisgw3.law.pace.edu/cases/960206a3.html>.

³⁵ Mohs, Article 64 927. 2016.

³⁶ A deferred payment credit means that payment takes place after the expiry of the designated period from shipment, from the bill of lading date or from presentation.

be opened 10 days before shipment but payment is only due 30 days after presentation of the documents under the letter of credit, some may argue that a fundamental breach exists if the buyer fails to open the letter of credit in time because it follows that he will not pay the price either. The hypothetical falls into the realm of Article 72(1) CISG, which entitles a party to declare the contract avoided if prior to the date of performance it is clear that one of the parties will commit a fundamental breach. In this case, however, we consider that the breach whose fundamentality is analysed regards the failure to pay the price or its likelihood (and not the failure to open the letter of credit). Accordingly, this scenario should be analysed due consideration of the buyer's obligation to pay the price and Article 25 CISG.

Damages

Liability for damages arises when a seller or a buyer breaches any of his obligations under the sales contract or the CISG.³⁷ The breach does not have to be a "fundamental" one under Article 25 CISG. The breach of any obligation by one of the parties, including the obligation to open a letter of credit,³⁸ triggers the right to damages that, under the principle of full compensation, shall be equal to the financial loss suffered by the other party because of the breach.³⁹ Therefore, damages recoverable are not related or limited to the amount of the letter of credit. The type of financial losses recoverable under the CISG include non-performance loss, incidental loss, and consequential loss resulting from the breach⁴⁰ of the obligation to open a letter of credit,⁴¹ which is independent from damages arising from the breach of the obligation to pay the contract price. For instance, where the delivery of the goods is subject to the issuance of letter of credit by the buyer's bank, any extra storage cost resulting from a deferred delivery of the goods because the buyer failed to provide the letter of credit in time shall be recoverable by the seller as damages.⁴²

³⁷ Articles 45(1)(b), 61(1)(b) and 74 CISG.

³⁸ Hossam A. El-Saghir, *The Interpretation of the CISG in the Arab World*, in CISG METHODOLOGY 366, 367, (André Janssen & Olaf Meyer eds., 2009).

³⁹ Ingeborg Schwenzer & Pascal Hachem, *The Scope of the CISG Provisions on Damages*, in CONTRACT DAMAGES—DOMESTIC AND INTERNATIONAL PERSPECTIVES 92, 93, (Djakhongir Saidov & Ralph Cunnington eds., 2008).

⁴⁰ Schwenzer, Article 74 1064. 2016.

⁴¹ BRUNO ZELLER, DAMAGES UNDER THE CONVENTION ON CONTRACTS FOR THE INTERNATIONAL SALE OF GOODS 70 (Oxford University Press 2nd ed. 2009): "a breach can occur even if it is not laid down explicitly in this Convention."

⁴² Schwenzer, Article 74 1067. 2016.

On the other hand, damages arising out of the bank's temporal or definite refusal to pay the amounts of the letter of credit to the beneficiary are not recoverable under the sales contract against the buyer. This case cannot be considered as a breach of the sales contract if, for example, the buyer has opened the agreed letter of credit and the bank has refused or delayed payment to the seller for reasons that could only be described as frivolous, untenable or spurious.⁴³ Any damage arising in such a case is recoverable under the bank and beneficiary legal relationship only.⁴⁴

RIGHT TO WITHHOLD PERFORMANCE

Article 71(1) CISG entitles a party to suspend the performance of its obligations, when it becomes apparent that the other party will not perform a substantial part of its obligations.⁴⁵ A party's right to suspend performance applies to concurrent performance by both parties, to agreed performance by the debtor first, as well as to performance by the creditor first.⁴⁶

It has been generally held that the right of suspension applies only to reciprocal obligations.⁴⁷ In other words, a creditor may only be entitled to withhold that obligation which constitutes the counterpart of the debtor's obligation that is likely to be unfulfilled. However, the right to suspension may also be extended to interdependent obligations, that is, those whose relation reflects that a party would not have agreed on the suspended obligation if the performance of a specific (probably nonreciprocal) obligation had not been promised in return.⁴⁸

In the context of letters of credit, the following questions arise. The buyer may have a contractual obligation to open a letter of credit prior or simultaneously to the delivery of the goods or the documents representing them. May the buyer withhold its obligation to open a letter of credit or even its (interdependent) obligation to pay the price if the buyer learns that the delivery will be delayed or the goods will be non-conforming ones?

Article 71 CISG requires the existence of threat of future failure to perform. This provision specifies the situations giving rise to an imminent breach of

⁴³ BRIDGE, 290, 291. 2013.

⁴⁴ *Id.* at 291, 292.

⁴⁵ DiMATTEO, 262. 2013; GARRO & ZUPPI, 290. 2012.

⁴⁶ Christiana Fountoulakis, *Article 71*, in SCHLECHTRIEM & SCHWENZER: COMMENTARY ON THE UN CONVENTION ON THE INTERNATIONAL SALE OF GOODS 1004, (Ingeborg Schwenzer ed. 2016).

⁴⁷ *Id.* at LOOKOFSKY, 144. 2012.

⁴⁸ Fountoulakis, 1004. 2016.

contract. A party's inability to perform shall be due to "a serious deficiency" or to "its creditworthiness" or to its "own conduct in preparing performance".⁴⁹ A "serious deficiency in the ability to perform" relates to factual elements such as strikes or impossibilities due to natural events as well as to legal impediments like failures due to government laws or action.⁵⁰ Generally, available information about basic market conditions or market developments that could possibly endanger performance is not an impediment within the meaning of Article 71(1)(a) CISG.⁵¹ Serious deficiency in "creditworthiness" relates to insolvency and similar events or by cessation of payment.⁵² It is a common view that the buyer's failure to open a letter of credit in time qualifies as grounds for suspension of the seller's obligation to deliver the goods or the documents related to them.⁵³ Finally, doubts about the buyer's ability to perform its obligation to open a letter of credit due to its "own conduct in preparing performance" may regard the buyer's lack of experience in international payments.

A party's failure must relate to a "substantial" part of that party's obligations. The standard of failure is, nevertheless, lower than the "fundamental" breach standard in Article 25 CISG.⁵⁴ This is due to the fact that the remedy granted by Article 71 CISG is preventive.⁵⁵ The contract's main obligations may have not been performed yet and the suspension of a party's obligation, *per se*, does not lead to the avoidance of the contract. What may be considered a substantial part of a party's obligation has to be determined in light of the sales contract's provisions as a whole and the creditor's reasonable expectations under the contract that were known or ought to be known by the other party.⁵⁶ In relation to this, an ICC Arbitral Tribunal ruled that the claimant's suspension of its obligation to open a letter of credit because of the seller's demand to increase the price of the latest purchase orders by 10 percent or 15 percent (in a

⁴⁹ HONNOLD, 352. 1999; Damien Nyer, *Withholding Performance for Breach in International Transactions: an Exercise in Equations, Proportions or Coercion?*, 18 PACE INTERNATIONAL LAW REVIEW 29, 76 (2006).

⁵⁰ Fountoulakis, 1009, 1010. 2016.

⁵¹ *Id.* at 1010.

⁵² *Id.*

⁵³ Florian Mohs, *Article 64*, *see id.* at 926 (See also Canada August 21, 2003 Supreme Court of British Columbia (*Mansonville v. Kurtz*) available at <http://cisgw3.law.pace.edu/cases/030821c4.html>).

⁵⁴ Christiana Fountoulakis, *Article 71*, *see id.* at 1008.

⁵⁵ UNCITRAL, Comments Art. 71. 2012.

⁵⁶ Fountoulakis, 1009. 2016.

framework agreement) was improper because it was “excessive and disproportionate.”⁵⁷ The Tribunal explained that under Art. 54 CISG, a refusal to open a letter of credit is tantamount to a total refusal to pay the purchase price and that since the disagreement related to 10 percent or 15 percent of the price only, the buyer could have at least advance the amount that was undisputed.⁵⁸

Against this background, the buyer will be entitled to suspend an agreed obligation to open a letter of credit if the seller has already failed to perform a related counter-obligation stipulated in the contract such as the obligation to send a notice of transport in a CISG contract subject to CIF, CFR, CIP, or CPT Incoterms, whereby the seller informs that the agreed goods have become available for transport.⁵⁹ Similarly, the buyer may withhold its contractual obligation to open a letter of credit if the seller breaches an agreed obligation to furnish a delivery or performance guarantee first. Where the buyer is contractually bound to open a letter of credit first, only a real threat that the seller will not furnish a correlated delivery guarantee or performance guarantee may entitle the buyer to withhold the opening letter of credit. A real threat may emerge when the financing bank has cut the seller’s credit line or when the parent company that usually acts as the guarantor has announced its liquidation or insolvency.

The buyer could also suspend a contractual obligation to open a letter of credit, as well as its main obligation to pay the price, if it learns from reliable sources that the seller will not perform its obligation to deliver the goods. This may be the case when the goods in question have been destroyed before delivery and the seller is definitely prevented from performing its obligation to deliver the goods. A party’s imminent failure to perform a substantial part of its obligation due to force majeure or impossibility under Article 79 CISG, does not preclude the other party’s right to suspend performance if the requirements of Article 71 CISG are met.⁶⁰

A question of major practical relevance is whether a buyer who has already performed its contractual obligation to open a letter of credit may order the bank to stop payment when it learns that the other party will not perform a correlated or an interdependent obligation. In other words, whether a party is

⁵⁷ ICC Arbitration Case No. 11849 of 2003 (Fashion products case) *available at* <http://cisgw3.law.pace.edu/cases/031849i1.html>; cited by Karton, *THE INTERNATIONAL AND COMPARATIVE LAW QUARTERLY*, 891, 892 (2009).

⁵⁸ *Id.*

⁵⁹ UNCITRAL, *Comments Art. 71*. 2012.

⁶⁰ BRUNNER, 376. 2008.

entitled to stop performance after performance under Article 71(2) CISG in the context of letters of credit. On this subject, some scholars submit that the right to stop performance after performance operates only on the seller's benefit and in relation to the delivery of goods since during the Vienna Conference the buyer's right to stop payment after being ordered was discussed but not included.⁶¹

Once the letter of credit is opened by the buyer, it loses any possibility to stop payment by the bank since the credit is paid under its own terms. The buyer has no inference in a relationship he created between the bank and the seller. Only if the terms of the letter of credit allow the buyer to revoke the letter of credit in light of the beneficiary's imminent threat of failure to perform the underlying contract, the buyer may rely on the exoneration afforded by Article 71(2) CISG: in that case the buyer will not incur in any breach under the underlying sales contract.

This being said, the letter of credit has its own mechanism to stop payment in cases where the seller breaches its obligations vis-à-vis the bank under the letter of credit itself (not under the CISG). This mechanism may be triggered by presentation of non-complying documents by the seller. It is a fundamental principle of documentary credits that only a complying presentation of documents by the seller must be honoured and this is known as the doctrine of compliance.⁶² If a bank honours a non-complying presentation, the bank will be liable to the buyer.⁶³ Therefore, the bank has a right to stop payment if the seller does not present the documents required under the letter of credit.⁶⁴ The practical application of the doctrine of compliance has given rise to a debate relating to the standard to be applied and whether the applicable standard is one of strict compliance or substantial compliance.⁶⁵ By referring to the general criterion of "complying presentation" in Articles 2, 15, and 16, the UCP 600 do not answer that question.⁶⁶ Occasionally the terms of the credit make provision as to the approach to be taken by the bank with respect to certain discrepancies; for instance, with respect to typing mistakes, etc. The Swiss

⁶¹ Fountoulakis, 1016. 2016.

⁶² BRIDGE, 277. 2013; Meral, ANKARA BAR REVIEW, 47 (2012); Cronican, McGEORGE LAW REVIEW, 388 (2013).

⁶³ BRIDGE, 288. 2013; the issuing bank will be liable to the buyer, or the confirming bank will be liable to the issuing bank.

⁶⁴ Art. 16(a) UCP 600.

⁶⁵ BRIDGE, 277. 2013; explaining that courts in England have endorsed the "strict compliance" standard. *See also* RAMBERG, 144. 2011; MUGASHA, 23. 2003.

⁶⁶ BRIDGE, 278. 2013.

Federal Supreme Court in a decision of January 11, 1989 took an approach departing from the doctrine of strict compliance.⁶⁷ In this case, the letter of credit stated that a receipt confirming the delivery of the goods had to be issued by an agent of the issuing bank (which is an unusual condition in itself). As such a receipt was missing, the confirming bank refused to pay. The Court held that such refusal was unconscionable, given that the delivery of the goods was not in dispute.⁶⁸

In addition, fraud by the seller will require the bank to stop payment of the letter of credit.⁶⁹ A request to pay in fraud regards the presentation by the seller of “documents that contain, expressly or by implication, material representations of fact that to his knowledge are untrue.”⁷⁰ The most common example may be the presentation of forged documents attesting that the goods have been delivered but in fact the goods were not delivered or have been delivered but without any value.⁷¹ But apart from the above scenarios, the bank’s duty to pay is an obligation independent of the contract of sale and is not subject to claims or defences by the buyer resulting from his relationship with the bank or the seller.⁷²

Pursuant to Article 71(3) CISG, the right of suspension or stoppage ceases to apply as soon as the debtor provides adequate assurances that it will perform.⁷³ For example, if the buyer fails to open a letter of credit, the seller is entitled to suspend the performance of his obligations until the buyer gives

⁶⁷ See Swiss Supreme Court January 11, 1989 BGE/ATF 115 II 67 = JdT 1989 I 342 available at http://relevancy.bger.ch/php/clir/http/index.php?lang=de&zoom=&type=show_document&highlight_docid=atf%3A%2F%2F115-II-67%3Ade.

⁶⁸ *Ibid.*

⁶⁹ Michelle Kelly-Louw, *Illegality as an exception to the autonomy principle of bank demand guarantees*, 42 THE COMPARATIVE AND INTERNATIONAL LAW JOURNAL OF SOUTHERN AFRICA, 348, 351 (2009); Gao, THE INTERNATIONAL LAWYER, 1070 (2007); Rodrigo, eLAW: MURDOCH UNIVERSITY ELECTRONIC JOURNAL OF LAW, 6, 7 (2011); Meral, ANKARA BAR REVIEW, 45 (2012); James G. Barnes & James E. Byrne, *Letters of Credit*, 67 THE BUSINESS LAWYER, 1286 (2012).

⁷⁰ Rodrigo, eLAW: MURDOCH UNIVERSITY ELECTRONIC JOURNAL OF LAW, 7 (2011): citing Lord Diplock in *United City Merchants (Investments) Ltd v Royal Bank of Canada (The American Accord)* [1983]1 AC 168.

⁷¹ Gao, THE INTERNATIONAL LAWYER, 1079 (2007).

⁷² Meral, ANKARA BAR REVIEW, 49 (2012).

⁷³ Canada August 21, 2003 Supreme Court of British Columbia (*Mansonville v. Kurtz*) available at <http://cisgw3.law.pace.edu/cases/030821c4.html>. In this case the seller relied expressly on article 71 CISG to justify its suspension of delivery due to the buyer’s failure to open a letter of credit. The Court concluded that there had been suspension and notification, as per article 71(3) CISG, but only during a two week period. Given that the equipment was eight

assurances.⁷⁴ Assurances may consist of other types of means to secure the underlying transaction such as mortgages, liens, chattel mortgage, assignments, etc.⁷⁵

RESTITUTION

In case of avoidance of the underlying contract, Article 81(2) CISG entitles a party who has performed its obligation to open a letter of credit to claim its return from the other party. If the letter of credit's moneys have already been paid without legal grounds at the time of avoidance, the reimbursement of such moneys may be claimed in accordance with the CISG provisions on the unwinding of the contract.

CONCLUSION

The CISG offers an effective legal framework for the enforcement of a buyer's obligation to open a letter of credit under an international sale of goods contract. The CISG's system of remedies strikes a balance between a seller's right to obtain the agreed promise of payment by a bank through a letter of credit and the economic benefit of maintaining the international sales contract alive in spite of the occurrence of a minor breach. In this line of thought, the seller will always be entitled to request the buyer to comply with an agreed obligation to open a letter of credit or to amend the nonconforming terms of one already opened. On the other hand, a party's right to avoid the contract will depend on whether or not the breach of contract is "fundamental" within the meaning of Article 25 or pursuant to the contract terms. In this regard, failure to open a letter of credit in time or after the additional period of time granted by the seller will lead to a right to avoid the contract where time is of the essence.

Depending on whether the threat of a future breach meets the requirements of Article 71 CISG, a buyer's failure to open a letter of credit will entitle the seller to suspend a related counter-obligation or even an interdependent obligation. Similarly, a buyer required to open a letter of credit prior or simultaneously to the delivery of the goods may suspend performance if there is a clear threat that the seller will not deliver.

The very nature of irrevocable letters of credit makes it impossible for a buyer to stop performance after the letter of credit has been opened under Article

weeks late in total, the Court found that the seller was in breach for having delivered six weeks late.

⁷⁴ Mohs, Article 64 926. 2016.

⁷⁵ Christiana Fountoulakis, *Article 71*, see *id.* at 1020.

71(2) CISG. But the letter of credit has its own rules that will allow a bank to stop payment in cases where the seller presents non-complying documents or there is fraud in the seller's request for payment.

To sum up, the CISG's provisions contribute to the effective enforcement of the fundamental bargain to which the parties under an international sales contract agreed to with a payment clause stipulating an obligation to open letter of credit: presentation of complying documents will enforce the bank's promise to pay for the buyer.

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