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IRREVOCABLE LETTERS OF CREDIT AND THE RESPONSIBILITY OF THE BANKS

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ABSTRACT

Purpose: *The purpose of this article is to explore the Irrevocable Letters of Credit and its importance. In addition to, the responsibility of the banks when dealing with these Irrevocable Letters of Credit and the events in which courts can intervene.* ***Methodology /approach:*** *This article has employed descriptive and comparative methods. The following materials were referenced as part of this article: books, journal articles, cases, reports, legislations.* ***Findings:*** *This article has found that letters of credits are very important in the field of international trade because they give fast and secure ways of payment, and grant sellers more protection if the letter of credit is confirmed by a bank. Also, it has discovered that the letter of credit is governed by two principles. First, the principle of autonomy, which means the underlying contact is independent of and separate from the letter of credit. Secondly, the doctrine of strict compliance, which means that a bank can reject documents that are presented by a seller if they not comply with the conditions of the letter of credit. Moreover, this article highlighted that the task of banks is to examine documents from their face, and without making an investigation. Moreover, this article has found that fraud exception seems to be the main exception in the doctrine of autonomy. Finally, it has shown that there is an approach which extends the fraud exception to include nullity exception which may improve the letter of credit.* ***Originality/value:*** *This article contributes to increase the understanding of the Irrevocable Letters of Credit and the responsibility of the banks when deal with these documents. In addition, it discovers the situations in which the court can intervene in Irrevocable Letters of Credit.*

KEYWORDS
irrevocable letter of credit, banks, revocable letter of credit, international commerce, autonomy, UN, UCP 600, fraud, nullity, illegality.

1. INTRODUCTION

The international transactions of sale of goods seem more difficult compared to the transactions within the boundary of one country because the buyer wants to receive the goods according to conditions of the contract before paying the consideration, whereas a seller is concerned about receiving the consideration in due time. (Carr, 2010) In other words, the seller needs to make clear that he will get the amount of goods or services; similarly, the buyer desires to pay against what was actually demanded (Marie, 2006). In fact, breaching is accepted from both. Frías García (2010,pp 69,70) states that' the possibility of either party's defaulting on the business transactions, the physical distance between parties, the different time zones and currencies, the need for additional intermediaries, the nature of multi- jurisdictional transaction and fact that parties do not know each other are reasons that explains the dominant role letters of credit'. Generally, the payment may be affected by many factors, such as the trust between the buyer and seller (Carr, 2010). Murray et al (2007) states that: 'letter of credit also called documentary credit or bankers commercial credits'; See also Article 2 of UCP 600 defines credit as: '… [a]ny arrangement, however named or described, that is irrevocable and thereby constitutes a definite undertaking of the issuing bank to honour a complying presentation'. Commonly, the basic means of payment include: open account, bill of exchange, documentary bill and letter of credit. The latter is vital in international commerce in (Intraco Ltd v. Notis Shipping Corpo 1981) the court held that 'Irrevocable letters of credit and bank guarantees given in circumstances such that they are equivalent to an irrevocable letter of credit have been said to be the life blood of commerce. Thrombosis will occur if, unless fraud is involved, the courts intervene and thereby disturb the mercantile practice of treating rights thereunder as being equivalent to cash in hand'. since the seller has confidence about his payment by the guarantor. In addition, the buyer may sue the bank for any damage, and may increase its funds from that bank against the fees. (Carr, 2010) Generally, the operation of a letter of credit consists of four stages:(a) A seller and a buyer agree about a contract of sale of goods (the underlying contract) and the payment through a letter of credit; (b) The buyer requests his bank called grantor to open a credit with particular conditions, in favour of the seller; (c) Issuing banking informs the seller that the letter of credit is opened, and will honour it if documents comply with requirements (García, 2010). Sometimes the issuing bank informs the seller through the advising bank or confirmed bank; (Carr, 2010) (d) While the seller presents documents in agreed time, the revocable letter of credit, and if it conforms with conditions, then will pay the consideration (Carr, 2010).

Moreover, there are four main types of letters of credit, including: (a) a revocable which is less reliable, therefore, the buyer can terminate it; (Chuah, 2005) (Cape Asbestos Co Ltd v Lloyds Bank Ltd 1921) In which the buyer informed the bank to revoke revocable letter of credit and inform the buyer. The bank forgot to inform the seller who sent the goods. The court held that the bank was not responsible for any damage and this notice should send by the buyer. (b)An irrevocable which cannot be cancelled by the buyer (Griffin et al 2003).It seems the Uniform Customs and Practice for Documentary Credits (UCP) (Janet Ulph, 2007), who states that ' The UCP was first issued by the International Chamber of Commerce (ICC) in 1933. It has been regularly revised since then in order to ensure that it reflected current banking and trade practice. The most recent version had been the UCP 500, promulgated by the ICC in 1993 and effective from January 1, 1994.3 The ICC Commission on Banking Technique and Practice (Banking Commission) initiated a fundamental review in 2003. After three years of preparation and consultation, unanimous approval of the draft was given by the Banking Commission on October 25, 2006'. Article 3 of UCP 600 considering that all letters of credits are irrevocable; Bridge (2007) states that 'A credit is irrevocable even if there is no indication to that effect' In contrast, Article 6 of UCP 500 states the two types. It has been argued that the revocable one seems not a real credit, therefore, the trend of UCP 600 appears more practicable; See also Article 2 of UCP 600 states that '…Credit means any arrangement, however named or described, that is irrevocable and thereby constitutes a definite undertaking of the issuing bank to honour a complying presentation...'. (c) a confirmed letter. Sometimes the correspondent bank confirms to seller opening letter, therefore the seller has right to claim this bank in his jurisdiction. (Carr, 2010) This may happen if the seller does not trust the issuing bank (Griffin et al 2003). Hooley (2003 states that: 'A letter of credit is separate from, and independent of, the underlying contract between the beneficiary and the applicant and the relationship between the issuing bank and the applicant. Thus, absent fraud (or possibly illegality), the beneficiary's breach of the underlying contract is no defence to the issuing bank (nor to the confirming bank). By the same token, the issuing bank cannot refuse to honour its undertaking just because of the applicant's failure to put it in funds'; See Also Article 2 of UCP 600 states that 'Confirmation means a definite undertaking of the confirming bank, in addition to that of the issuing bank, to honour or negotiate

a complying presentation'. Finally, an unconfirmed one, which happens if the advising bank just informs the seller (Griffin et al 2003). In this research Article 5 of UCP 600 will be discussed critically. It provides that 'Banks deal with documents and not with goods, services or performance to which the documents may relate', in light of relevant cases.' Which includes the principle of the autonomy and the doctrine of strict compliance. Finally, exceptions of autonomy which include fraud chiefly, and another possible exception which contain a nullity and illegality.

2. THE PRINCIPLE OF THE AUTONOMY

The principle of the autonomy means a letter of credit is independent of, and separate from, an underlying contract which is financed by the letter of credit. Malek QG et al (2009) state that '' The bank should not take account of any other than the terms of credit and the documents which are presented to it. This is subject to the possible exception…''. Therefore, generally a bank only deals with documents, not commodities or services as to the relationship with others parties involved in the letter of credit (Burnett and Vivienne 2009). To put it another way, the bank does not concern itself with an underlying contract (M. Bridge, 2007). Hence, banks should make decision based on documents only to accept or reject it in specific time (Paul, 2002). Generally, any conflict may arise between a vendor and a purchaser as to the agreement of sale, it will not affect the letter of credit, (Carr, 2010). and a purchaser could not block the payment, however, he only has the option to make a claim before a court (Chuah, 2005). This doctrine is mentioned in Article 4 and 5 of UCP 600 which latter states, 'Banks deal with documents and not with goods, services or performance to which the documents may relate'. Furthermore, Article 4 (a) of UCP 600 declares that the letter of credit is independent from the agreement of sales. It has been pointed out that Article 5 of UCP 500 states that "In Credit operations all parties concerned deal with documents and not with goods, services and/or performances to which the documents may relate". In contrast to, Article 5 of 600 omits the phrase 'all parties' because a buyer and a seller usually deal with goods. It should be emphasised that banks while dealing with the documents, must follow the procedures mentioned in UCP 600 (Ebenezer, 2009). "The problem of non – documentary conditions is addresses in UCP by Article 14 (h)" (Malek QG et al 2009, 178). Article 14 (h) of UCP 600 states that "If a credit contains a condition without stipulating the document to indicate compliance with the condition, banks will deem such condition as not stated and will disregard it".

Furthermore, it is commonly accepted that ruining the principle of the autonomy of credit may lead to the destruction of trade confidence (M. Bridge 2007). This principle is confirmed in many cases. For instance, in Discount Record Ltd v Barclay Bank Ltd. And Another. In which a buyer, upon arrival the goods, discovered that some boxes contained nothing, and others contained cassettes instead of records (Discount Records Ltd. V. Barclays Bank Ltd. And Barclays Bank International Ltd. 1975). At that time the representative of the issuing bank was attending (Discount Records Ltd. V. Barclays Bank Ltd. And Barclays Bank International Ltd. 1975). Then the buyer tried to get an injunction to prevent the bank from buying the amount. The court stated that, what was provided by the plaintiff was considered just an allegation of fraud, (Discount Records Ltd. V. Barclays Bank Ltd. And Barclays Bank International Ltd. 1975) and an injunction would not be granted unless there was an adequately serious reason for doing so. Seemingly, the decision of the court was unfair with regard to the plaintiff, and required a high standard of evidence, since the facts showed intentional fraud. Moreover, this fraud was discovered in attendance of the representative of the issuing bank (Discount Records Ltd. V. Barclays Bank Ltd. And Barclays Bank International Ltd. 1975). It has been argued that the respect for the principle of autonomy does not mean to protect dishonest sellers. Furthermore, if the buyer has not a case against issuing bank it might be in a poor position to sue the seller who is in another country (Bridge 2007). It has been declared that: 'Sticking to the general non-interference approach, English courts have saddled plaintiffs with a great burden of proof, requiring them to establish the existence of "clear" or "obvious" fraud.' (Ross P. Buckley and Xiang Gao, 2002).

Moreover, this principle was supported in Urquhart Lindsay & Co. Ltd v. Eastern Bank, Ltd. In this case, a letter of credit was opened with a specific amount (£70.000) and the parties agreed to increase the price if the labour increased. The buyer discovered invoices containing additional costs. The issuing bank refused to pay the extra amount. The seller cancelled the contract and sued the bank. The court declared in favour of the plaintiffs, based on the fact that the bank undertook to pay the amount without conditions (Urquhart Lindsay & Co. v. Eastern Bank, Ltd. 1922). It appears that the seller complied with the terms of the letter of credit when tendered an invoice. However, it seems that when the bank applied, the buyer's instructions did not concern what exactly was written in the letter of credit. In other words, when documents complied with the letter of credit the bank has to honour them (A. C. Epps and R. Harvey Chappell 1952). It appears that the decision was accurate and in favour of the principle of the autonomy.

Furthermore, in (Hamzeh Malas and Sons v British Imex Industries Ltd. 1958). A purchaser claimed the goods were imperfect and sought an injunction. The court pointed out that when the bank opened a confirmed letter of credit this established obligation between the bank and the seller, and the bank should pay without considering any disputes between the seller and buyer with regard to goods related to the agreement or not. The seller believed, under the confirmed letter, that he would receive his money. The letter stated that: An elaborate commercial system has been built up on the footing that bankers' confirmed credits are of that character, and, in my judgment, it would be wrong for this court in the present case to interfere with that established practice…, as I see it, would break down completely if dispute as between the vendor and the purchaser was to have the effect of 'freezing', if I may use that expression, the sum in respect of which the letter of credit was opened.' (Hamzeh Malas and Sons v British Imex Industries Ltd. 1958, 129).

This decision appears more accurate as to the importance of the letter of credit and obligations of a bank toward a seller, and the court firmly declared not interference as to letter of credit in case disputes as to an underlying contract. In addition, the confirmed one is most secure for seller (Campbell, 2008).

Furthermore, in (Power Curber International Ltd. v. National Bank of Kuwait 1982) Lord Denning pointed out that it is important that a bank, when issued the letter of credit, must discharge its obligations, without concerning any dispute between the buyer and seller in relation to goods, since the letter of credit as a Bill of Exchange is presented as consideration of goods. The court very firmly stated to keep it separate from the underlying contract because it does not permit making deductions or making counterclaims with regard to the letter of credit (Power Curber International Ltd. v. National Bank of Kuwait 1982). In short, the abovementioned decisions of UK courts appear how far the letter of credit independent from underlying contacts. Generally, the UK courts are very reluctance to interfere therein because it plays a vital role in trade. Therefore, no counter claim will be accepted as to the letter of credit, and generally the bank has to pay.

3. THE PRINCIPLE OF STRICT COMPLIANCE

A seller must submit documents that conform strictly with the conditions of the letter of credit to the issuing or conformed bank or advising banks, as appropriate (Paul, Bills of lading and bankers' documentary credits 2007). Subject to this doctrine, when a bank receives documents can reject the ones that are not in strict compliance with the requirements of the letter of credit (Carr, 2010). The cause behind this principle is that a bank deals with documents only and has no relation with goods or services. It is not required from a bank to make an investigation. Furthermore, these documents may include invoices, bills of lading, and certificates of quality (Michael and Michael, 2007). Moreover, it should be noted that the level of care required from banks as to examining documents is reasonable care (Carr, 2010), according to Article 13 (a) of UCP 500 which states: 'Banks must examine all documents stipulated in the credit with reasonable care, to ascertain whether or not they appear, on their face, to be in compliance with the terms and conditions of the Credit...'. In contrast, Article 14 (a) of UCP 600, does not state that the duty of care is required. It has been argued that the responsibility of a bank may become a strict liability. In other words, the hypothesis is that the bank is liable unless proven otherwise (Michael and Michael, 2007).

Furthermore, the bank is considered as an agent of the seller. Therefore, there is a legal and contractual duty which should be carried out by the bank. Nevertheless, banks have to carry out obligations and exercise reasonable care as applies in common law (Ebenezer, 2009). Moreover, the greatest risk for the bank is that, although there are inconsistencies with documents, it may make payment to the beneficiary. However, a bank may protect itself from this risk by two ways: making a payment upon the indemnity of the beneficiary covers the bank from any claim that may arise from the buyer, based on non-conformity between the documents that were submitted and the conditions of the letter of credit. Secondly, a bank may accept to pay under reserve; nevertheless, there is common agreement about the definition of under reserve, generally determined according to the intention of the various parties (Carr, 2010). In (Banque de l'Indochine et Suez SA v JH Rayner (Mincing Lane) Ltd 1983) a confirmed bank, before paying, declared that 'effected under reserve due to the discrepancies', the court explained that: it means a contract under which the beneficiary undertakes to repay the amount if the issuing bank refused the documents. It should be noted that if a bank desires to make payment subject to under reserve it must consider all elements to make an accrete contract, for instance: acceptance, offer, and competent parties, since there is no particular definition.

Moreover, a bank may accept to pay based on wrong action and become liable, as was illustrated in (Equitable Trust Company of New York v Dawson Partners Ltd 1927). The defendant agreed with the plaintiff to open a letter of credit in favour to a seller, according to conditions of the letter of credit, a certificate of quality shall be given by experts. In other words, a certificate would be given by more than one expert. Due to miscommunication between the issuing bank and the advising bank, the latter asked the seller to provide the certificate to be issued by one expert. The shipment was made and the amount was paid to seller. Then, the defendant discovered that the goods were fraudulent. The court held that: '... [i]f the bank does as it is told, it is safe; if it declines to do anything else, it is safe; if it departs from the conditions laid down, it acts at its own risk' (Equitable Trust Company of New York v Dawson Partners Ltd 1927, 52). Furthermore, this court determined that: '[o]ne of the conditions on which the defendant undertook to reimburse the plaintiff – namely that there should be … a certificate of quality to be issued by experts – has not been complied with'. Clearly, the requirements of the buyer should be respected by a bank otherwise the banks are considered responsible for that. In addition, it seems that in trade, some goods may require more opinion to make an assessment and this may reduce the possibility of the fraud.

Furthermore, another court applied this principle in (J.H.Rayner & Co Ltd v. Hambros's Bank Ltd 1943). A contract of sale was created between an English seller and a Danish buyer. Payment was made through an irrevocable letter of credit opened by the defendant bank. The goods described in the letter of credit were about 1400 tons of 'Coromandel groundnuts'. However, the bill of lading characterised the goods as 'machine-shelled groundnut kernels' whose usage was meant to be 'Coromandel groundnuts'. The Court of Appeal declared that the defendant had rightly refused payment on the grounds that the documents submitted did not comply with the conditions of the credit. It seems the decision of the court in favour of the principle of strict compliance. It has been argued that, it appears so difficult to a bank to examine the documents and make comparison with customs of trade in particular field. In addition, the role of the bank is to deal with documents only.

Moreover, in (Seaconsar Far East Ltd v Bank Markazi Jomhouri Islami Iran 1993). A letter of credit required plainly that each document should contain a letter of credit number and a name of buyer, however, one document did not comply. It was declared that the bank had the right to reject the documents (Seaconsar Far East Ltd v Bank Markazi Jomhouri Islami Iran 1993).Moreover, the court pointed out that a typographical mistake is considered as minor defect. Apparently, when the buyer makes conditions clearly, the seller and the bank should comply with said conditions. In addition, one may argue that this trend of rigidity may obstruct the letter of credit (Carr, 2010). Consequently, UCP 600 permits slight differences. For instance, in Article 14(e), apart from commercial invoices, does not require other documents be complied, but not conflict. Moreover, Article 14 (d) of UCP 600 is considered more practicable because it does not require documents to be identical. To put it another way, a bank may accept non-identical documents if they do not contradict anything within the context of the letter of credit and international banking customs. However, the international standard banking practice is not clear. Therefore, conflicts may arise with experts over any dispute (Michael and Michael, 2007). In contracts, Article 13(a) of UCP 500, requires documents to be identical with others. This situation led to the refusal of many documents by a bank (Michael and Michael, 2007).

Moreover, in (Fortis Bank S.A./N.V. and (2) Stemcor UK Ltd v Indian Overseas Bank 2011), five letters of credit opened for the seller and three of them were confirmed and paid by the confirming bank. However, the issuing bank refused to pay the other two and the amount due to the confirming bank who alleged that there were discrepancies. The court held that even if there were discrepancies the issuing bank had an obligation to pay since it failed to rerun documents to the confirmed bank 'with reasonable promptness' (Fortis Bank S.A./N.V. and (2) Stemcor UK Ltd v Indian Overseas Bank 2011, 35). It has been argued that letters of credit under UCP 600 must be examined within five banking days under Article 61 (d) of UCP 600. However, this decision seems important since there is an emphasis on the time factor as a defence and a seller may rely on it in relation to the principle of strict compliance (Choo, 2010). Furthermore, it should be highlighted that a bank should examine documents within a specific duration because time is so important in business, therefore, Article 14 (b) of UCP 600 provided that a bank has to decide on documents during a maximum of five banking days. It differs from Article 13 (b) of UCP 500, which stated that banks should examine documents within a reasonable time not exceed seven banking days.

4. THE EXCEPTIONS OF THE PRINCIPLE OF AUTONOMY

The doctrine of autonomy is important as above-mentioned. However, based on public interest or to protect the innocent party (Ross P. Buckley and Xiang Gao 2002), there are exceptions to this principle which include fraud as main exception, and possible a nullity and illegality (Frías García, 2010; Gabriel and Peter, 2006). Nevertheless, not any allegation may be accepted to stop the payment by a bank. Generally, there is debate about the standards of proof of fraud which are required (Gabriel: Peter, 2006). Gabriel and Peter (2006) stated that the fraud exception was first decided in (Sztejn v. J. Henry Schroder Banking Corpn 1941). In this case the claimant alleged that the supplier was not complying with the terms of the agreement and sent worthless goods and asked to prevent the bank from paying under documentary letter. The court held that an adjunction could be issued if fraud was deliberate and the bank has known about vendor's fraud before the drafts and documents have been tendered for payment, the court declared that 'In such a situation, where the seller's fraud has been called to the bank's attention before the drafts and documents have been presented for payment, the principle of the independence of the bank's obligation under the letter of credit should not be extended to protect the unscrupulous seller' (Sztejn v. J. Henry Schroder Banking Corpn 1941, 634). This decision was criticised since it did not explain the level of knowledge required to enable the bank to refuse the payment. This decision was criticised as' A difficulty arising from this case is that it is not clear whether this was a case of false documents or rather a case of fraud in the underlying transaction' (Dixon 2004, 391). It may argue that the court did not require any standard; therefore, any knowledge based on facts may be sufficient. Moreover, it appears that the advantage in this case is that the court clearly confirmed the obligation of the bank, subject to the principle of the autonomy did not extend to cover a dishonest seller. However, the court considered the duty of banks to deal with documents, therefore if the bank knew after paying, it will not be responsible. Therefore, this decision appears in favour of a weak party (buyer) and supports the trust in the letter of credit itself.

Furthermore, *in* (Bolivinter Oil S.A. v Chase Manhattan Bank 1984)the clear acknowledgment with regard to 'fraud exception' was stated by Sir John:

The wholly exceptional case where an injunction may be granted is where it is proved that the bank knows that any demand for payment already made or which may thereafter be made will clearly be fraudulent. But the evidence must be clear, both as to the fact of fraud and as to the bank's knowledge (Bolivinter Oil S.A. v Chase Manhattan Bank 1984, 393).

It has been criticised that the standard of fraud required by the UK courts is very high since they required that the evidence of fraud should be obvious as to fact establishes it and the bank's awareness (Xiang and Buckley, 2003). Therefore, the buyer may not able to fulfil these conditions. Moreover, the question remains open about degree of clarity that is required. This reflects the trend of this court's reluctance to interfere in letters of credit in order to save this mechanism. Furthermore, if the seller does not become involved in fraud a bank may be required to pay. For instance, in (United City Merchants (Investments) Limited v. Royal Bank of Canada 1983), a contact made between an English company and a Peruvian company stated that the payment method shall be a letter of credit and the shipment should be on 15 December, 1976. The false date put by the agent of the shipping company and the seller was not involved in the fraud. The Court of Appeal held that the bank had the right to refuse the payment since documents appeared on the face of it to be false and, expropriate any legal effect. However, did not consider as a nullity (United City Merchants (Investments) Limited v. Royal Bank of Canada 1983). Furthermore, in the House of Lords, Lord Diplok preferred to leave open the matter of rights of the innocent beneficiary as to documents forged by third party, and he refused this decision by reasoning that the false date put by the agent of the shipping company and the seller was not involved in the fraud. There are no reasons to refuse to pay the amount since the document 'was far from being a nullity.' (United City Merchants (Investments) Limited v. Royal Bank of Canada 1983, 188).

Moreover, Chuah (2005) criticised that the knowledge of the seller was not required to apply the fraud exception since fraud made the document entirely nullified. It has been argued that a forged document does not comply with the principle of strict compliance. Furthermore, this decision may lead to an increase of using forged documents in letters of credit. Moreover, there is no reason to deal with the seller preferentially since he has the right to sue the wrongdoer.

Furthermore, the general nullity exception is discussed in (Montrod Ltd v. Grundkotter Fleischvertriebs GmbH and Standard Chartered Bank 2001) in which a letter of credit stipulated that inspection certificates should be signed by a representative of Montrod. However, three certificates were signed by a beneficiary because he thought he had been authorised. The court declared that the bank should pay since the beneficiary acted not fraudulently and in good faith (Montrod Ltd v. Grundkotter Fleischvertriebs GmbH and Standard Chartered Bank 2001). However, Potter L.J. pointed out that: 'In my view there are sound policy reasons for not

extending the law by creation of a general nullity exception' (Montrod Ltd v. Grundkotter Fleischvertriebs GmbH and Standard Chartered Bank 2001, 335). These reasons include: it may lead to destroy the letter of credit system, harm the beneficiary when the good faith element was not considered, increase the duty of banks to investigate documents in contracts which are not required under UCP 500, and there is no authority under common law (Montrod Ltd v. Grundkotter Fleischvertriebs GmbH and Standard Chartered Bank 2001). Nevertheless, Hooley Richard criticised that this decision may enhance dealing with forged documents in international commerce, fake documents do not conform with letters of credit, and forged documents offer nothing secure for banks (Richard 2002). It has been argued that there is a precedent in common law as to nullity international trade (Motis Exports Ltd v Dampskibsselskabet Af 1912 Aktieselskab and Aktieselskabet Dampskibsselskabet Svendborg 1999). It should be pointed out that if a document is nullified because it is forged by a beneficiary, it seems non – controversial, therefore, this act is considered an offence (Nelson, 2011).

Furthermore, some commentators, against nullity exception for the same reasons, abovementioned by Potter L.J. (Nelson 2011). Generally, it may be useful to adopt a nullity exception in order to enhance the reliance of letters of credit. It seems this trend has been adapted by a Singaporean court (Donnelly, 2008). Moreover, it appears that UCP 600 does not put guidelines to courts and banks as to the nullity (García, 2010). Therefore, it has been suggested that rules may be required to state situations in which courts and banks may refuse to pay the amount equivalent with the UN Convention on Independent Guarantees and Stand-by Letters of Credit, which specifies events in which courts can issue an injunction, and banks can refuse to honour, guarantee or stand-by a letter of credit. Article 19 of this Convention shows that there is no obligation to payment, for instance, if it is clear any document is not genuine or has been forged, the amount is not due according to documents or the failure of implementation of underlying contract because of the intentional misbehaviour by a beneficiary. As Lord Diplock highlighted; 'It is unsupported by authority. It provides a further complication where simplicity and clarity are needed. There are problems in defining when a document is a nullity (United City Merchants (Investments) Limited v. Royal Bank of Canada 1983, 168).'

Moreover, despite Lord Diplock's refusal to accept illegality as an exception in (United City Merchants (Investments) Limited v. Royal Bank of Canada 1983). Clearly the illegality exception is accepted in the recent case, (Mahonia Ltd v JP Morgan Chase Bank And other 2003). In this case, Mohonia borrowed an amount to Enron Corporation. Repayment ensured by a letter of credit issued by WestLB AG. Enron failed to guarantee repayment. Then WestLB AG was asked to pay the amount, according to the letter of credit. The bank rejected allegations that the letter of credit was infected by illegality, since Enron did comply with United States Securities Laws (Mahonia Ltd v JP Morgan Chase Bank And other 2003). Based on public policy the court held that the illegality affected underlying transactions and the letter of credit (Mahonia Ltd v JP Morgan Chase Bank And other 2003). As a result, questions may arise as to the duty of a bank, for instance, is a bank liable to investigate main transactions? Does a bank have the ability to deal with specifications mentioned in an underlying contact (Carr, 2010)? It seems banks are not obliged to go beyond the letter of credit and are not responsible for any falsification or originality. Generally, some argue that courts sharply increase events of exception, and therefore, may destroy letters of credit (García, 2010). On the other hand, others argued that generally a buyer sometimes waives the discrepancies and there are not many letters of credits affected by courts (García, 2010). Nevertheless, a balance among all parties and international guidelines to courts are required.

5. CONCLUSION

Letters of credits seem very important in the field of international commerce because they give fast and secure ways of payment, and grant sellers more protection if the letter of credit is confirmed by a bank. In addition, it ensures documents conform with the conditions of a buyer. However, the letter of credit is governed by two principles. First, the principle of autonomy, which means the underlying contact is independent of and separate from the letter of credit. Secondly, the doctrine of strict compliance, which means that banks can reject documents that are presented by a seller if they not comply with the conditions of the letter of credit. Furthermore, the task of banks is to examine documents from their face, and without making an investigation. Additionally, the duty required from a bank is the duty of care. Moreover, this article has found that fraud exception seems to be the chief exception in the doctrine of autonomy. Considering fraud exception in UK courts, hard standards of proof are required since conditions of this expectation demand that the facts of fraud must be clearly established of which a bank has knowledge, and moreover, the beneficiary is not involved therein. This exception improves to include an illegality, which is criticised since it is very vague. However, UK courts refused a nullity exception, which may be accepted by other courts.

In addition, this article has illustrated that there is an approach which extends the fraud exception to include nullity exception which may enhance the letter of credit. Moreover, this article has suggested that a balance is required among all parties involved in the letter of credit, in order to enhance trust. As efforts which have been carried out as to UN Convention on Independent Guarantees and Stand-by Letters of Credit.

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