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[2004] EWHC 129, 4 February 2004

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LETTER OF CREDIT – APPLICABLE LAW AND *FORUM NON CONVENIENS*

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The facts

Marconi, an English company, claimed damages against Panin Bank, an Indonesian bank, for breach of contract in respect of the latter's failure to honour its obligations as a confirmer of letter of credit. The letter of credit was issued in respect of certain consignments of telephone equipment delivered to an Indonesian company, PT Prismasentra Agung. The total contract price was $14,221,972.60. The letter of credit was issued by Hastin Bank (also an Indonesian bank) and confirmed by Panin Bank. On receipt of shipping documents, Panin Bank passed them on to Hastin Bank but Hastin Bank refused to pay, relying on certain discrepancies. Panin Bank, in turn, refused to accept the drafts which had been drawn upon it relying on the same discrepancies. It was accepted by the court that the reasons given by Hastin Bank were arguably unjustified. In the meantime, Hastin Bank had become insolvent.

Marconi claimed that Panin Bank had wrongfully failed to accept bills of exchange properly drawn upon it and presented to it under the terms of the letter of credit. Marconi was granted leave to serve the claim form out of jurisdiction on Panin Bank.

Panin Bank applied to set aside service and asked for a declaration that the English court had no jurisdiction over Panin Bank. The issue was thus one of *forum non conveniens*, the Brussels Regulation having no application as the defendant was domiciled in Indonesia, not in an EU Member State.

The decision

The court had to be satisfied that at least one of the grounds listed in CPR r6.20 provided a good arguable case for permission to serve out of the jurisdiction to be granted. Marconi asserted that the contract between Panin Bank, as confirming bank, and Marconi, as beneficiary, was made within the jurisdiction and that the contract was made by Standard and Chartered Bank (London) which acted as Panin Bank's agent for the purpose of advising the confirmation to Marconi. It was also submitted by Marconi that the letter of credit was governed by English law and the failure to honour the credit constituted a breach within the jurisdiction. Panin Bank's response was that the letter of credit was governed by Indonesian law.

An obvious starting point for the decision was whether the letter of credit was governed by English law. David Steel J relied on the Rome Convention as contained in the Contracts (Applicable Law) Act 1990 and held that, on balance, the governing law of the credit was English law. Be that as it may, the court went on to hold that even if the credit was not governed by English law, there was a good arguable case that the contract was made in the jurisdiction where the confirmation was conveyed or that the contract was made by an agent trading or residing in the jurisdiction as Standard Chartered Bank, at least under English law (*Bank Melli Iran v Barclays Bank* [1951] 2 Lloyd's Rep 362), might be properly deemed to be Panin Bank's agent in advising the confirmation of the letter of credit.

The fourth ground relied on by Marconi in its application to serve out was that the failure to pay out under the letter of credit amounted to a breach occurring in the jurisdiction. The bank, on the other hand, contended that the obligation to pay was on Panin Bank, which was resident in Indonesia and the decision to refuse payment was taken in Indonesia. The judge, however, was unconvinced that this necessarily meant that the breach had occurred in Indonesia. The judge opined that it was arguable the bank was required to pay in London because either negotiation was to take place there or payment was to be effected through Standard Chartered Bank as the collecting bank. Thus, there was a good arguable case for service out on that ground.

The final issue for the court was whether it was permissible to execute alternative service on Panin Bank's solicitors in London. The court concluded that although it was not impractical to serve on Panin Bank in Indonesia, it would involve very extensive delay. Under Indonesian law, the procedure for service could take at least one year during which time there was no prospect for the claimant being able to enforce its claim against the defendant. Although there is authority from the Court of Appeal in *Knauf UK GmbH v British Gypsum Ltd* [2002] 1 WLR 907 that a mere desire for speed was unlikely to amount to good reason justifying alternative service 'since claimants nearly always desire speed', that case concerned a claimant who was concerned to steal a march on the defendant by trying to short-circuit the normal procedure under the Hague Convention in order to gain priority under Article 21 (of the Brussels Convention) over the defendant. That was not the case here.

Comment

As far as the application of CPR r6.20 is concerned, this case does not offer much that is new but in respect of the jurisprudence on the applicable or proper law of the letter of credit, David Steel J's observations make for interesting analysis. In order to determine the applicable law of the credit, it is vital to refer to the Rome Convention. The Convention provides in general that the parties' choice of law agreement will be given effect to. However, most letters of credit do not contain a choice of law clause. That absence means that the court should turn to the presumptions in Article 4 of the Convention to ascertain the law of the country with the closest connection with the credit. Article 4 provides:

> (2) Subject to the provisions of paragraph 5 of this Article, it shall be presumed that the contract is most closely connected with the country where the party who is to effect the performance which is characteristic of the contract has, at the time of the conclusion of the contract, his habitual residence, or in the case of a body corporate or unincorporated, its central administration. However, if the contract is entered into in the course of that party's trade or profession, that country shall be the country in which the principal place of business is situated or, where under the terms of the contract the performance is to be effected through a place of business other than the principal place of business, the country in which that other place of business is situated.
>
> (5) Paragraph 2 shall not apply if the characteristic performance cannot be determined, and the presumptions in paragraphs 2,3 and 4 shall be disregarded if it appears from the circumstances as a whole that the contract is more closely connected with another country.

It was only natural for Panin Bank to argue that paragraph (2) applied squarely because the characteristic performance was the payment on presentation of documents and as that was to be carried by the bank, the country with the closest connection with the credit must be presumed to be Indonesia where the bank is situated. The bank contended that there was nothing in the circumstances which would suggest that the presumption in paragraph (2) should be disregarded.

The bank relied on Mance J's judgment in *Bank of Baroda v Vysya Bank* [1994] 2 Lloyd's Rep 87. It might be recalled that in that case, the credit was issued by Vysya Bank, an Indian bank and confirmed by Bank of Baroda's branch in London. Under Article 4(2), the applicable law of the contract between the confirming bank and the beneficiary was English law because the characteristic performance was the honouring of the letter of credit by the confirming bank's branch office and that branch was situated in England. However, by applying Article 4(2) to the contract between the issuing bank and the beneficiary, that applicable law would be Indian law because the party to effect the characteristic performance, namely the provision of the finance service, was the Indian bank. Mance J, however, was concerned that would increase the conflicting decisions being given because there would be more than one applicable law in the contractual matrix. His Lordship thus considered that Article 4(5) should be applied to the relationship between the issuing bank and the beneficiary. As the issuing bank's obligation is customarily the reimbursement of the confirming bank, the latter's relationship with the beneficiary is pivotal.

In *Bank of Baroda*, the relationship in question was that between the issuing bank and the confirming bank. Although in the present case, the relationship in question was that between the confirming bank and the beneficiary, as Panin Bank rightly contended, the principle to be drawn from *Bank of Baroda* was that the characteristic performance was the honouring of the letter of credit and that was to be performed by Panin Bank. David Steel J, however, did not think that the analogy was conclusive. His Lordship reasoned that Article 4(2) should in fact be derogated from because as the credit was communicated to Marconi by an England-based bank, Standard Chartered Bank, and that Standard Chartered Bank was contemplated as one of several negotiating banks for the drafts drawn under the letter of credit, England had the same closeness with the contract as Indonesia. The court also added that even if Standard Chartered Bank did not negotiate the drafts drawn under the credit, it acted as collecting bank in checking and forwarding the documents.

A significant argument raised by Panin Bank was that Standard Chartered Bank was not a confirming bank, it was merely an advising bank with a relatively minor role in the letter of credit. It might not even be a negotiating bank. In this connection, David Steel J turned to the pre-Convention case of *Offshore International SA v Banco Central SA* [1977] 1 WLR 399 for support. That case stated that it would cause great inconvenience to apply the law of the issuing bank as the proper law where the actual payment obligation under the letter of credit was to be met by another bank in a different jurisdiction. There, the letter of credit was issued by a Spanish bank and was advised, but not confirmed, by a New York bank. Payment was to be made in US dollars against documents presented in New York. Ackner J held:

> . . . on the side of New York [law] are all matters of performance, whereas, in relation to Spanish law, Spain and a Spanish bank was the source of the obligation. In my judgment, it is with New York law that the transaction has its closest and most real connection. Moreover . . . I am satisfied that . . . very great inconvenience would arise, if the law of the issuing bank was to be considered the proper law. The advising bank would have constantly to be seeking to apply a whole variety of foreign laws.

The reliance on this great inconvenience is used to support the argument that the fact that there was no confirmation by Standard Chartered Bank was immaterial. There is one important difference between that and the present case. There, it was clearly expected that the New York bank was to act also as the negotiating bank. It is less clear in the present case. Indeed, although Panin Bank had authorized the drafts to be negotiated by any bank in England, the understanding was that Marconi was to be paid directly by them. Payment was to be made by Panin Bank through the agency of its correspondent bank in London. Should a distinction be made between payment to be effected through a negotiating bank and direct payment through the international banking system? It seems implicit from the present case that there was no distinction to be made on such lines as long as payment was to be effected in England. Where that is the case, there was a good arguable case that English law is the applicable law of the credit.

As regards the emphasis on the great inconvenience to be caused by holding the law of the issuing bank as the applicable law, two points may be made. First, it is not certain how relevant that consideration is, given the terms of Article 4(2) of the Convention. Secondly, the inconvenience should not be overstated. The rights and obligations of the parties in a letter of credit will to a large extent be governed by the UCP 500 (and the ISBP 98 (International Standard Banking Practice)). National courts are slow to depart from the Guidelines and Opinions of the ICC. Indeed, many letter of credit disputes would have been referred to the ICC national committees for resolution. The standardization of the rules and principles applicable to letters of credit should not make matters too inconvenient even though a foreign law is applied. The problem with the present case is not one primarily in relation to the choice of law, but the choice of jurisdiction – Marconi was keen to bring the matter within English jurisdiction by tying the application to the issue of applicable law. It might also be added that the fact that the letter of credit is governed by the law of the place where payment is made (as held in the present case and *Bank of Baroda*) does not mean that contending with foreign law is necessarily totally ameliorated. The drafts (bills of exchange) which the banks negotiate could very well be governed by a different applicable law depending on where it was drawn (section 72 Bills of Exchange Act 1882); although the problem is not likely to be significant because most of such drafts will be drawn in England, that is not a foregone conclusion.

In *Bank of Baroda* which was followed in the present case, the judicial attitude to Article 4(5) is that it holds equal, if not stronger, force with Article 4(2). Under Article 4(5), the court has the discretion to disregard the presumption in Article 4(2). Cheshire and North (13th ed, p 574) refers to *Société Nouvelle des Papeteries de l'Aa v Machinefabriek* (BOA 25 September, NJ (1992) No750, RvD (1992) No 207) a Dutch decision to show the difference in attitude between the English and Dutch courts. In the Dutch case, the Dutch Supreme Court refused to apply Article 4(5) to rebut the presumption that Dutch law applied, even though the only connection with the Netherlands was that it was the place of business of the person whose performance was characteristic of the contract, whereas many elements of the case linked the contract to France, including the vital fact that performance of the contract (by that person) took place there. Cheshire and North said:

> . . . perhaps more worrying is the underlying difference in attitude in England and the Netherlands towards the whole question of rebuttal of the presumption. The English attitude is that Article 4(5) formally makes the presumption very weak and the presumption is displaced if the court considers

> that it is not appropriate to apply in the circumstances of any given case . . . In contrast, the Dutch attitude is that the presumption is of great weight and should only be rebutted in exceptional cases, that Article 4(2) is the main rule . . . and that the law identified by the presumption prevails unless it has no real significance as a connecting factor.

The present case reaffirms that English attitude. It would be useful for the ECJ to offer guidance on how the presumptions should be applied.

JC