

How to Use This Supplement

This 2007 Supplement brings the Fourth Edition of *The Law of Letters of Credit* up to date and serves both as a means of keeping the main volume current and as a reference to recent developments.

Each entry in the supplement is keyed to a chapter, paragraph (§), and specific page number in the main volume. An italicized instruction line indicates where the new material belongs in relation to text or footnotes in the main volume. To check for new developments on a point discussed in the main volume, find the corresponding paragraph number in the supplement. The sequences of the main volume and supplement are identical, and the top of each supplement page carries a paragraph reference. Cross-references marked “this supplement” refer to new material in the supplement; cross-references to “main volume” refer to the Fourth Edition, as updated by the supplement.

The supplement treats all recent, important letter of credit cases and literature, among them cases and articles dealing with:

- **Forum non conveniens.** Resolving a split in the circuits, the U.S. Supreme Court has ruled that a letter of credit beneficiary’s action against a carrier for falsely backdating a bill of lading was better tried in Chinese courts and that the U.S. District Court did not have to determine whether it had jurisdiction before rendering the forum non conveniens ruling. See §§ S11.02[1][b], S11.02[8].
- **The beneficiary’s interest in a letter of credit prepayment.** One court cautions the purchaser of a bankruptcy debtor’s leases and “related security deposits” that the purchaser has no interest in standby credits and collateral securing the debtor’s reimbursement obligation. See §§ S7.03[3][a], S7.03[3][k].
- **The limits on treating letters of credit as cash.** Sometimes, letters of credit are sound substitutes for cash, but sometimes they aren’t. See §§ S1.06, S3.07[2].
- **The curious notion that draws on a standby damage the reputation of the applicant.** An Australian court joins the list of those who think an applicant’s reputation must be protected from draws even when there is a bona fide dispute in the underlying transaction. See §§ S2.03[2], S7.04[1].
- **Applicant recovery for wrongful draws.** Although the courts are not precise in defining the reasons for their holdings, evidence continues to mount that when a beneficiary has no right in the underlying contract to

draw on the credit and retain the proceeds, the court will order return of the funds to the applicant. Conversely, courts are disinclined to allow an applicant to recover credit proceeds from a beneficiary that drew with full right to draw under related documents. *See* ¶ S7.03[3][1].

- **Lender liability for bank’s termination of letter of credit not limited by economic loss doctrine.** Lenders must often make quick judgments about defaulting borrowers, but haste coupled with what a jury found to be overbearing conduct can lead to serious consequences—\$20.3 million in compensatory damages and another \$7 million in punitive damages, neither of which awards were subject to the limitations of the economic loss doctrine, one court held. Yet, another court rejected the borrower’s claim for recovery when the lender reduced the line of credit after collecting serious loan closing costs and imposed a substantial early loan termination fee. *See* ¶ S7.07.
- **Allocating attorney fees in complex litigation.** UCC Article 5 commands courts to award attorney fees to the prevailing party in an action in which “a remedy is sought” under Article 5. In some cases, the provision creates significant allocation problems. In other cases, it seems, courts simply ignore the legislative command that there be an award of such fees. *See* ¶ S9.09.
- **Assigning a principal obligation as an assignment of letter of credit rights.** It is a well-established feature of real estate and personal property security law that assignment of a secured obligation entails assignment of the mortgage/security interest with it. In letter of credit law, a letter of credit often serves as a supporting obligation, and assignment of it constitutes an assignment of “letter of credit right” but not of the right to draw on the credit. *See* ¶¶ S10.03[2], S10.04[2][a].
- **Evergreen clauses.** An evergreen clause should contain a provision allowing the *issuer* to cancel the credit on notice to the *beneficiary*, not the other way around. *See* ¶¶ S5.03[3][e], S5.03[3][f].
- **Damages for wrongful dishonor.** Article 5 limits damages for wrongful dishonor to the face amount of the credit, but one case finds a cause of action for “breach of statutory duty” that might give rise to additional damages. *See* ¶ S9.02[5].
- **Breach of warranty and wrongful draw.** Some foreign jurisdictions do not recognize the letter of credit warranty; but when there is a wrongful draw, they use letter of credit warranty analysis. *See* ¶¶ S6.07[1], S9.04[3].

- **More wrongful draws.** Sometimes, a draw on a letter of credit is innocent, and the applicant will have a cause of action in breach of warranty or breach of contract; but at other times, the draw is made with no honest belief that the money is due, and the applicant will have a cause of action in fraud or deceit. *See* ¶¶ S9.03[1][c], S9.04[3].
- **The fraud exception to the independence principle.** It will disconcert some, especially those taking letters of credit from Australian banks, to read language in judgments from Australian courts reflecting less than serious interest in keeping the fraud exception narrow. *See* ¶¶ S7.04[4][d], S11.05[3][b][iv].
- **Waivers.** An applicant may always waive documentary discrepancies, but that right in the applicant does not create a correlative right in the beneficiary to obtain payment against defective documents, as one beneficiary argued to no avail. *See* ¶ S6.06[2].
- **Parties to the letter of credit obligation.** Contrary to what may be dictum in one case, the applicant is not a party to the letter of credit. *See* ¶¶ S2.08[1], S9.02[4].
- **Standby letter of credit as supersedeas bond.** Letters of credit are usually less expensive than bonds, but one court is unwilling to approve a standby letter of credit in lieu of a supersedeas bond on the basis of cost savings alone. The bond, this court holds, is “superior” from the appellant’s perspective. *See* ¶ S1.06.
- **Protecting innocent parties.** Innocent purchasers of the beneficiary’s draft or demand for payment may qualify for protection from injunctions when the beneficiary has practiced fraud or is otherwise subject to valid reasons for stopping payment of the credit. Courts have not always limited the protection to those who take the drafts or demand *for value*. They should. *See* ¶¶ S8.02[2], S8.02[3].

To ensure easy access to new developments, the supplement contains Cumulative Tables of UCC Sections, UCP, and Cases, as well as a Cumulative Index; these tables and index include references to both the main volume and the supplement.

Consult *The Law of Letters of Credit* only in conjunction with the supplement.

