

BILL ANALYSIS

Senate Research Center

S.B. 547
By: Carona
Economic Development
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As Filed

DIGEST

Currently, Chapter 5 of the Business & Commerce Code (Article 5 of the Uniform Commercial Code (UCC)) deals with the rights and obligations created by a letter of credit. A letter of credit is a definite undertaking by an "issuer" to a "beneficiary" to make a payment upon the beneficiary's presentation of the documents listed in the issuer's undertaking. The official sponsors of the UCC, the American Law Institute (ALI) and the National Conference of Commissioners on Uniform State Laws (NCCUSL), have proposed a series of amendments to Article 5 in order to enhance the commercial acceptability of letters of credit. The recommendations both clarify the legal obligation of issuers to pay promptly and harmonize Article 5 with modern commercial practices with respect to letters of credit, including the increasing use of electronic communication. This bill would revise the Texas enactment of Article 5 with the series of amendments recommended by ALI and NCCUSL.

PURPOSE

As proposed, S.B. 547 revises the Texas enactment of Article 5 of the Uniform Commercial Code (UCC) (Chapter 5, Business & Commerce Code), relating to letters of credit, with a series of amendments recommended by the official sponsors of the UCC, the American Law Institute and the National Conference of Commissioners on State Laws.

RULEMAKING AUTHORITY

This bill does not grant any additional rulemaking authority to a state officer, institution, or agency.

SECTION BY SECTION ANALYSIS

SECTION 1. Amends Chapter 5, Business & Commerce Code, as follows:

CHAPTER 5. LETTERS OF CREDIT

Sec. 5.101. **SHORT TITLE:** Uniform Commercial Code--Letters of Credit.

Sec. 5.102. **New heading: DEFINITIONS.** Defines "advisor," "applicant," "beneficiary," "confirmer," "dishonor," "document," "good faith," "honor," "issuer," "letter of credit," "nominated person," "presentation," "presenter," "record," and "successor of beneficiary." Provides that the definitions of "accept" or "acceptance" in Section 3.409, Business & Commerce Code, and "value" in Sections 3.303 and 4.211, Business & Commerce Code, apply to this chapter. Provides that Chapter 1, Business & Commerce Code, contains certain additional general definitions and principles of construction and interpretation applicable throughout this chapter.

Sec. 5.103. **SCOPE.** Provides that this chapter applies to letters of credit and to certain rights and obligations arising out of transactions involving letters of credit. Provides that the statement of rule in this chapter does not by itself require, imply, or negate application of the same or a different rule to a situation not provided for, or to a person not specified, in this chapter. Provides that with the exception of certain subsections of this chapter, the effect of this chapter may be varied by agreement or by a provision stated or incorporated by reference in an undertaking. Provides that a term in an agreement or undertaking generally excusing

liability or generally limiting remedies for failure to perform obligations is not sufficient to vary obligations prescribed by this chapter. Provides that rights and obligations of an issuer to a beneficiary or a nominated person under a letter of credit are independent of the existence, performance, or nonperformance of a contract or arrangement out of which the letter of credit arises or which underlies it, including contracts or arrangements between the issuer and the applicant and between the applicant and the beneficiary. Deletes provisions setting forth the prior scope of this chapter. Deletes text of existing Sections 5.102 and 5.103.

Sec. 5.104. New heading: FORMAL REQUIREMENTS. Authorizes a letter of credit, confirmation, advice, transfer, amendment, or cancellation to be issued in any form that is recorded and is authenticated by a signature or in accordance with the agreement of the parties or the standard practice referred to in Section 5.108(e) of this chapter. Deletes provisions relating to signature requirements for a credit.

Sec. 5.105. CONSIDERATION. Provides that consideration is not required to issue, amend, transfer, or cancel a letter of credit, advice, or confirmation. Deletes a prior provision providing that no consideration is required to establish credit.

Sec. 5.106. New heading: ISSUANCE, AMENDMENT, CANCELLATION, AND DURATION. Provides that a letter of credit is issued and becomes enforceable according to its terms against the issuer when the issuer sends or otherwise transmits it to the person requested to advise or to the beneficiary. Provides that a letter of credit is recoverable only if it so provides. Provides that after a letter of credit is issued, rights and obligations of a beneficiary, applicant, confirmer, and issuer are not affected by an amendment or cancellation to which that person has not consented except to the extent the letter of credit provides that it is revocable or that the issuer may amend or cancel the letter of credit without that consent. Provides that if there is no stated expiration date or other provision that determines its duration, a letter of credit expires one year after its stated date of issuance or, if no date is stated, after the date on which it is issued. Provides that if a letter of credit that states that it is perpetual expires five years after its stated date of issuance or, if no date is stated, after the date on which it is issued. Deletes existing text.

Sec. 5.107. New heading: CONFIRMER, NOMINATED PERSON, AND ADVISOR. Provides that a confirmer is directly obligated on a letter of credit and has the rights and obligations of an issuer to the extent of its confirmation. Provides that the confirmer has rights against and obligations to the issuer as if the issuer were an applicant and the confirmer had issued the letter of credit at the request and for the account of the issuer. Provides that a nominated person who is not a confirmer is not obligated to honor or otherwise give value for a presentation. Authorizes a person requested to advise to decline to act as an advisor. Provides that an advisor that is not a confirmer is not obligated to honor or give value for a presentation. Provides that an advisor undertakes to the issuer and to the beneficiary accurately to advise the terms of the letters of credit, confirmation, amendment, or advice received by that person and undertakes to the beneficiary to check the apparent authenticity of the request to advise. Provides that even if the advice is inaccurate, the letter of credit, confirmation, or amendment is enforceable as issued. Provides that a person who notifies a transferee beneficiary of the terms of a letter of credit, confirmation, amendment, or advice has the rights and obligation of an advisor under this section. Provides that the terms in the notice to the transferee beneficiary may differ from the terms in any notice to the transferor beneficiary to the extent permitted by the letter of credit, confirmation, amendment, or advice received by the person who so notifies. Deletes existing text.

Sec. 5.108. New heading: ISSUER'S RIGHTS AND OBLIGATIONS. (a) Requires an issuer to honor a presentation that appears on its face strictly to comply with the terms and conditions of the letter of credit, except as otherwise provided in Section 5.109. Requires an issuer to dishonor a presentation that does not appear to comply, except as otherwise provided in Section 5.113 and unless otherwise agreed with the applicant.

(b) Provides that an issuer has a reasonable time after presentation, but not beyond the end

of the seventh business day of the issuer after the date of its receipt of document to honor, to accept a draft to incur a deferred obligation, or to give notice to the presenter of discrepancies in the presentation.

(c) Provides that an issuer is precluded from asserting as a basis for dishonor any discrepancy if timely notice is not given or any discrepancy not stated in the notice if timely notice is given, except as provided in this section.

(d) Provides that failure to give notice specified in this section or to mention fraud, forgery, or expiration in the notice does not preclude the issuer from asserting as a basis for dishonor fraud or forgery or expiration of the letter of credit before presentation.

(e) Requires an issuer to observe standard practice of financial institutions that regularly issue letters of credit. Provides that determination of the issuer's observance of the standard practice is a matter of interpretation for the court. Requires the court to offer the parties a reasonable opportunity to present evidence of the standard practice.

(f) Provides that an issuer is not responsible for the performance or nonperformance of an underlying contract, arrangement, or transaction; an act or omission of others; or observance or knowledge of the usage of a particular trade other than the standard practice referred to in this section.

(g) Requires an issuer to disregard the nondocumentary conditions and treat them as if they were not stated if the undertaking constituting a letter of credit contains nondocumentary conditions.

(h) Requires an issuer who has dishonored a presentation to return the documents or hold them at the disposal of, and send advice to that effect to, the presenter.

(i) Sets forth the conditions an issuer that has honored a presentation is entitled to or precluded from taking. Deletes existing text of Section 5.108.

Sec. 5.109. FRAUD AND FORGERY. Sets forth instances in which an issuer is required to honor the presentation if a presentation is made that appears on its face strictly to comply with the terms and conditions of the letter of credit, but a required document is forged or materially fraudulent, or honor of the presentation would facilitate a material fraud by the beneficiary on the issuer or applicant. Sets forth instances in which a court of competent jurisdiction is authorized to temporarily or permanently enjoin the issuer from honoring a presentation or grant similar relief against the issuer or other persons if an applicant claims that a required document is forged or materially fraudulent or that honor of the presentation would facilitate a material fraud by the beneficiary on the issuer or applicant. Deletes existing text.

Sec. 5.110. New heading: WARRANTIES. Sets forth certain warranties a beneficiary warrants if its presentation is honored. Deletes existing text of Sections 5.110-5.114.

Sec. 5.111. REMEDIES. (a) Authorizes the beneficiary, successor, or nominated person presenting on its own behalf to recover from the issuer the amount that is the subject of the dishonor or repudiation if an issuer wrongfully dishonors or repudiates its obligations to pay money under a letter of credit before presentation. Authorizes the claimant to obtain specific performance or, at the claimant's election, recover an amount equal to the value of performance from the issuer, if the issuer's obligation under the letter of credit is not for the payment of money. Authorizes the claimant to recover incidental but not consequential damages. Provides that the claimant is not obligated to take action to avoid damages that might be due from the issuer under this section. Requires the claimant's recovery from the issuer to be reduced by the amount of damages avoided. Requires the issuer to prove the amount of damages avoided. Provides that in the case of repudiation, the claimant need not present any document.

(b) Authorizes the applicant to recover damages resulting from the breach if an issuer wrongfully dishonors a draft of demand presented under a letter of credit or honors a draft or demand in breach of its obligation to the applicant.

(c) Authorizes a person to whom the obligation is owed to recover damages resulting from the breach less any amount saved as a result of the breach if an advisor or nominated person other than a confirmer breaches an obligation under this chapter or an issuer breaches an obligation not covered in Subsection (a) or (b). Provides that a confirmer has liability of an issuer specified in Subsections (a) and (b) to the extent of the confirmation.

(d) Requires a person who is found liable under Subsection (a), (b), or (c) to pay interest on the amount owed thereunder from the date of wrongful dishonor or other appropriate date.

(e) Requires reasonable attorney's fees and other expenses of litigation to be awarded to the prevailing party in an action in which a remedy is sought.

(f) Authorizes the damages that would otherwise be payable by a party for breach of an obligation under this chapter to be liquidated by agreement or undertaking in an amount or by a formula that is reasonable in light of the harm anticipated. Deletes existing Section 5.115.

Sec. 5.112. New heading: TRANSFER OF LETTER OF CREDIT. Provides that except as provided in Section 5.113, the right of a beneficiary to draw or otherwise demand performance under a letter of credit may not be transferred. Authorizes the issuer to refuse recognition or carry out the transfer under certain conditions, even if a letter of credit provides that it is transferrable. Deletes provision that provides that the right to draw under a credit can be transferred or assigned only when the credit is expressly designated as transferable or assignable. Makes conforming changes.

Sec. 5.113. TRANSFER BY OPERATION OF LAW. (a) Authorizes a successor of a beneficiary to consent to amendments, sign and present documents, and receive payment or other items of value in the name of the beneficiary without disclosing its status as a successor.

(b) Authorizes a successor of a beneficiary to consent to amendments, sign and present documents, and receive payment or other items of value in its own name as the disclosed successor of the beneficiary. Requires, except as provided by this section, an issuer to recognize a disclosed successor of a beneficiary as beneficiary in full substitution for its predecessor upon compliance with the requirement for recognition by the issuer of a transfer of drawing rights by operation of law under the standard practice referred to in this chapter or in compliance with other reasonable procedures sufficient to protect the issuer.

(c) Provides that an issuer is not obliged to determine whether a purported successor is a successor of a beneficiary or whether the signature of a purported successor is genuine or authorized.

(d) Provides that honor of a purported successor's apparently complying presentation under this section has the consequences specified in Section 5.108. Provides that documents signed in the name of the beneficiary or of a disclosed successor by a person who is neither the beneficiary nor the successor of the beneficiary are forged documents for the purposes of Section 5.109.

(e) Authorizes an issuer whose rights of reimbursement are not covered by Subsection (d) or substantially similar law and any confirmer or nominated person to decline to recognize a presentation under Subsection (b).

(f) Provides that a beneficiary whose name is changed after the issuance of a letter of credit

has the same rights and obligations as a successor of a beneficiary under this section.

Sec. 5.114. ASSIGNMENT OF PROCEEDS. (a) Defines "proceeds of a letter of credit."

(b) Authorizes a beneficiary to assign its right to part or all of the proceeds of a letter of credit. Authorizes the beneficiary to do so before presentation as a present assignment of its right to receive proceeds contingent upon its compliance with the terms and conditions of the letter of credit.

(c) Provides that an issuer or nominated person need not recognize an assignment of proceeds of a letter of credit until it consents to the assignment.

(d) Provides that a consent may not be unreasonably withheld if the assignee possesses and exhibits the letter of credit and presentation of the letter of credit is a condition to honor.

(e) Provides that rights of a transferee beneficiary or nominated person are independent of the beneficiary's assignment of the proceeds of a letter of credit and are superior to the assignee's right to the proceeds.

(f) Provides that neither the rights recognized by this section between an assignee and an issuer, transferee beneficiary, or nominated person nor the issuer's or nominated person's payment of proceeds to an assignee or a third person affect the rights between the assignee and any person other than the issuer, transferee beneficiary, or nominated person. Provides that the creation and perfection of a security interest in or granting an assignment of a beneficiary's right to proceeds is governed by Chapter 9 or other law. Provides that against persons other than the issuer, transferee beneficiary, or nominated person, the rights and obligation arising upon the creation of a security interest or other assignment of a beneficiary's right to proceeds and its perfection are governed by Chapter 9 or other law. Deletes existing text of Section 5.116.

Sec. 5.115. STATUTE OF LIMITATIONS. Sets forth the statute of limitations for a cause of action to enforce a right or obligation arising under this chapter.

Sec. 5.116. CHOICE OF LAW AND FORUM. (a) Provides that the liability of an issuer, nominated person, or advisor for action or omission is governed by the law of the jurisdiction chosen by an agreement in the form of a record signed or otherwise authenticated by the affected parties in the manner provided in this chapter or by a provision in the person's letter of credit, confirmation, or other undertaking. Provides that the jurisdiction whose law is chosen need not bear any relation to the transaction.

(b) Provides that unless Subsection (a) applies, the liability of an issuer, nominated person, or advisor for action or omission is governed by the law of the jurisdiction in which the person is located. Sets forth provisions regarding a person's location at the time of the undertaking. Provides that for the purpose of jurisdiction, choice of law, and recognition of interbranch letters of credit, but not enforcement of a judgment, all branches of a bank are considered separate judicial entities, and a bank is considered to be located at the place where its relevant branch is considered to be located under this subsection.

(c) Provides that the liability of an issuer, nominated person, or advisor is governed by any rules of custom or practice to which the letter of credit, confirmation, or other undertaking is expressly made subject. Sets forth conditions under which the rules of custom and practice govern when there is conflict between those rules and this subsection.

(d) Provides that if there is conflict between this chapter and Chapter 3, 4, 4A, or 9, Business & Commerce Code, this chapter governs.

(e) Authorizes the forum for settling disputes arising out of an undertaking within this chapter to be chosen in the manner and with the binding effect that governing law may be chosen in accordance with Subsection (a).

Sec. 5.117. New heading: SUBROGATION OF ISSUER, APPLICANT, AND NOMINATED PERSON. (a) Provides that an issuer that honors a beneficiary's presentation is subrogated to the rights of the beneficiary to the same extent as if the issuer were a secondary obligor of the underlying obligation owed to the beneficiary and of the applicant to the same extent as if the issuer were the secondary obligor of the underlying obligation owed to the applicant.

(b) Sets forth the subrogated rights of an applicant that reimburses an issuer.

(c) Sets forth the subrogated rights of a nominated person who pays or gives value against a draft or demand presented under a letter of credit.

(d) Sets forth conditions under which the subrogated rights granted in this section arise. Provides that until that time, the issuer, the nominated person, and the applicant do not derive under this section present or prospective rights forming the basis of a claim, defense, or excuse. Deletes existing text of Section 5.117.

SECTION 2. Amends Section 1.105b, Business & Commerce Code, to make conforming changes.

SECTION 3. Amends Section 2.512(a), Business & Commerce Code, to make conforming changes.

SECTION 4. Amends Section 9.103(a), Business & Commerce Code, to make conforming changes.

SECTION 5. Amends Section 9.104, Business & Commerce Code, to make conforming changes.

SECTION 6. Amends Section 9.105(c), Business & Commerce Code, to make conforming changes.

SECTION 7. Amends Section 9.106, Business & Commerce Code, to make conforming changes.

SECTION 8. Amends Sections 9.304 and 9.305, Business & Commerce Code, as follows:

Sec. 9.304. New heading: PERFECTION OF SECURITY INTEREST IN INSTRUMENTS, DOCUMENTS, PROCEEDS OF A WRITTEN LETTER OF CREDIT, AND GOODS COVERED BY DOCUMENTS; PERFECTION BY PERMISSIVE FILING; TEMPORARY PERFECTION WITHOUT FILING OR TRANSFER OF POSSESSION. Makes a conforming change.

Sec. 9.305. WHEN POSSESSION BY SECURED PARTY PERFECTS SECURITY INTEREST WITHOUT FILING. Makes conforming changes.

SECTION 9. Effective date: September 1, 1997.

SECTION 10. Makes application of this Act prospective.

SECTION 11. Emergency clause.