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Regulation of Letter of Credit in Ethiopia: A Critical Appraisal of the Law and Practice In Light Of International Recommendations

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**REGULATION OF LETTER OF CREDIT IN
ETHIOPIA: A CRITICAL APPRAISAL OF THE LAW
AND PRACTICE IN LIGHT OF INTERNATIONAL
RECOMMENDATION**

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JUNE, 2018

REGULATION OF LETTER OF CREDIT IN ETHIOPIA: A
CRITICAL APPRAISAL OF THE LAW AND PRACTICE IN
LIGHT OF INTERNATIONAL RECOMMENDATION

Thesis

Submitted in Partial Fulfillment of the Requirements for the Degree of
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By

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June, 2018



Thesis approval page

The thesis titled “*Regulation of Letter of Credit in Ethiopia: A Critical Appraisal of the Law and Practice in lite of international recommendation*” by Khalid Kebede is approved for the degree of Master of Laws (LL.M)

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Declaration

I, the undersigned, declare that the thesis comprises my own work. In compliance with widely accepted practices, I have duly acknowledged and referenced all materials used in this work. I understand that non-adherence to the principles of academic honesty and integrity, misrepresentation/fabrication of any idea/data/fact/source will constitute sufficient ground for disciplinary action by the University and can evoke criminal sanction from the State and civil action from the sources, which have not been properly cited or acknowledged.

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List of abbreviations and Acronyms

CBE	Commercial Bank of Ethiopia
ERCA	Ethiopia Revenue and Custom Authority
eUCP	Uniform Customs and Practice for Documentary Credits for Electronic Presentation
FDRE	Federal Democratic Republic of Ethiopia
ICC	International Chamber of Commerce
ISBP	International Standard Banking
L/C	Letter of Credit
NBE	National Bank of Ethiopia
UCC	Uniform Commercial Code
UCP500	Uniform Customs and Practice for Documentary Credits, 1994 Revision, ICC Publication no. 600 ("UCP")
UCP600	Uniform Customs and Practice for Documentary Credits, 2007 Revision, ICC Publication no. 600 ("UCP")
UK	United Kingdom
UNICTRAL	United Nations Commission on International Trade Law
USA	United States of America
UCP	Uniform Customs and Practice for Documentary Credits
URR	Uniform Rules for Bank-to-Bank Reimbursements under Documentary Credits
SWIFT	Society for World Wide Inter-bank Financial Tele-communication

CHAPTER ONE

INTRODUCTION

1.1. Background of the Study

Letter of credit, sometimes called documentary credit, documentary letter of credit, commercial credit, credit or L/C,¹ is generally understood as an arrangement in which a bank (issuing Bank) at the request and in accordance with the instruction of its customer (applicant) undertakes to pay a third party (beneficiary) a sum of money or accept a draft or other demands drawn so long as the documents are presented in line with terms and conditions of the credit.²

Import and export trade across national boundaries brings several risks both to the seller and the buyer. The risks include, but not limited to, risks resulting from long distance between the contracting parties, lack of information about solvency of the parties, divergent law and business practices, different currencies, difficult communication systems, transportation difficulties, and political upheavals.³ Letter of credit enhanced the international commercial transactions among traders residing in geographically distant places and who do not know each other by creating security and certainty among themselves that otherwise cannot be existed because of the risk of insecurity inherent in the international business transaction.⁴ Specifically, it assures the sellers (exporter) swift payment upon presentation of the required documents to the advising or conforming bank. On the other hand, the buyer (importer) also avoids the risk of paying the entire purchase in advance without knowing the seller is complying with the underlying contract.⁵

Letter of credit is considered as “the life blood of international commerce.”⁶ It is the first method of payment which transform the over lasting traditional usage of the international commercial

¹ Zhang Ruiqiao, *A Comparative Study of the Fraud Exception Rule of Letters of Credit Proposed Amendments to the Chinese Credit System*, LLM Thesis, McGill University, School of Law, 2009, p. 1 [Herein after Zhang, *A comparative study of fraud exception*]

² *Black's Law Dictionary*, 8th ed., s. v. “letter of credit”

³ Andreas Karl, *Letters of Credit and the Doctrine of Strict Compliance*, LL.M Thesis, University of Uppsala, School of Law, 2003, pp. 12-13 [Herein after Karl, *Letters of Credit and the Doctrine of Strict Compliance*]

⁴ Ch'ng Huck Yong, ‘International Trends in Documentary Credit Transactions’, *Sing. L. Review*, 2003, Vol. 14, pp. 171-219, at p. 171 [Herein after Ch,ng, *International Trends in Documentary Credit Transactions*]

⁵ Zsuzsanna Tóth, *Documentary Credits in International Commercial Transactions with Special Focus on the Fraud Rule*, PHD Dissertation, Pázmány Péter Catholic University, Faculty of Law and Political Sciences, 2006, p.1 [Herein after Zsuzsanna, *Documentary Credits in International Commercial Transactions*], p. 1

⁶ *Id.*, p. 17

transaction from “Money and goods” into “money and documents.”⁷ Hence, no need of actual delivery of the goods for the seller to get paid and the buyer to acquire the ownership title against goods under voyage. For that, in the business community there is a perception that, “no financial instrument is more vital to international commerce than the letter of credit.”⁸

Coming to Ethiopia, after the re-introduction of market led economic policy in the post 1991⁹, the import and export transactions are increased significantly.¹⁰ According to the report of National Bank of Ethiopia (herein after NBE), Ethiopian goods import and export transactions in the 2016/2017 Annual year shows significant increase compared to previous years. Specifically the import and export accounts \$15.8 Billion and \$ 2.9 Billion respectively.¹¹ There are different efforts to advance the increasing import and export transactions in Ethiopia among other things, by modernizing the payment systems. Currently Ethiopian banking practice devised various schemes of payment and financing for international business transactions, namely; letter of credit, cash against document, telegraphic transfer, advance payment, open account and the like.¹² Among these payment mechanisms, however, letter of credit is considered as the most secured and popular one.¹³

Despite the long ago mercantile history of letter of credit in the international commerce since the time of Ancient Egypt and Babylon¹⁴, it is introduced in much shorter times in Ethiopia. It is recognized as banking business since the introduction of modern banking in Ethiopia, 1905. Practically speaking, however, letter of credit become more operational and popular in the 1990s and onward.

The laws regulating letter of credit in Ethiopia is also a recent phenomenon. The landmark legislation in this regard is the 1960 Commercial Code of Ethiopia (herein after the Commercial

⁷ Lijia Yi, *Documentary Fraud under Letters of Credit: A Comparative Study of English and Chinese Law*, Master Thesis, Lund University, Faculty of Law, 2012, p. 3

⁸ Stephen J. Leacock, ‘Fraud in the International Transaction: Enjoining Payment of Letters of Credit in International Transactions’, *Vanderbilt Journal of Transnational Law*, 1984, Vol. 17, pp. 885-924, at p. 992

⁹ Solomon Abay Yimer, *Financial Market Development, Policy and Regulation: The International Experience and Ethiopia’s Need for Further Reform*, PHD Dissertation, University of Amsterdam, Faculty of Law, 2001, p. 1

¹⁰ NBE, 2015/2016, *Annual Report [of the National Bank of Ethiopia] 2015/2016 (Ethiopian Fiscal Year 2008)*, Addis Ababa, 2015/16, p. 56

¹¹ NBE, 2016/2017, *Annual Report [of the National Bank of Ethiopia] 2015/2016 (Ethiopian Fiscal Year 2009)*, Addis Ababa, 2016/17, pp. 46-57 [Herein after NBE, 2016/2017 Annual Report]

¹² U.S. Department of Commerce International Trade Administration, “International commerce payment mechanisms” at <<https://www.trade.gov/publications/pdfs/tfg2008ch1.pdf>> [Last accessed 7 April, 2018]

¹³ Interview with Ato Gezu Ayele Mengstu, Banking law Legal Advisor and legal service Manager at Addis International Bank, on *the letter of credit operation and legal framework in the Ethiopian*, March 4, 2018

¹⁴ Zsuzsanna, *Documentary Credits in International Commercial Transactions*, p. 1

Code). It introduces regulatory frameworks for letter of credit operations. It deals with the matter under, Book IV of the code. It allots nine provisions, from article 959 through 967. Articles on this section of the Code are verbatim copy of the 1951 version of the Uniform Customs and Practice for Documentary Credits (herein after UCP).¹⁵

Apart from the Commercial Code, regulatory rules can be found under the 1960 Civil Code of Ethiopia (the Civil Code)¹⁶ and various Directives of NBE and some other legislations.

In the current Ethiopian legal framework, letter of credit transactions are characterized as banking businesses and exclusively given to banking institutions.¹⁷ According to the Directives of NBE, any import and export transaction more than \$5000 should be processed through Letter of Credit or Cash against Document.¹⁸ In another Directive NBE added that foreign exchange approval for import and export payment shall only be on the basis of letter of credit.¹⁹ These show, despite existence of other modes of payment, letter of credit become favorable payment instrument in Ethiopia. The banking practice also suggests the same that majority of import and export transactions are processed through the instrument of letter of credit.²⁰

1.2. Statement of the Problem

Ethiopia as a country that looks forward for economic development, advancement of its import and export transactions to the level the international commercial community demands cannot be an option. One of the primary instruments to do so is modernization of its payment mechanisms, specifically its letter of credit. Indeed, in every annual year, billions of dollars are transacted through letter of credit in Ethiopia.²¹ That makes the instrument vital to the Ethiopian economy. However, proper functioning of letter of credit cannot be maintained and improved without

¹⁵ Tilahun Teshome *et al.*, *Position of the Business Community on the Revision of the Commercial Code*, Addis Ababa Chamber of Commerce and Sectoral Associations, Addis Abeba, 2008, p. 79 [Herein after Tilahun *et al.*, *Position of the Business Community*]

¹⁶ Civil Code of the Empire of Ethiopia, 1960, *Negarit Gazeta*, Extraordinary issue, Proclamation No.165, 19th year. No. 1, Article 1676 and 1678 [Herein after the Civil Code of Ethiopia]

¹⁷ Banking Business Proclamation, 2008, *Federal Negarit Gazeta*, Proclamation No. 592, 14th Year, No. 57, Article 2(2) [Herein after The Banking Business Proclamation of Ethiopia]

¹⁸ FXD/07/1998, National Bank of Ethiopia, Directive to Transfer NBE's Foreign Exchange Functions to Commercial Banks Directive No. FXD/07/1998, 18 August 1998, Article 5.4 cum 5.3 and 5.1 [Herein after Directive No. FXD/07/1998]

¹⁹ FEC/43/97, National Bank of Ethiopia, Exchange Control Directive Regarding Trade Transactions between Ethiopia and Eritrea Directive No. FEC/43/97, 19 December, 1997, Article 2(1) [Herein after Directive No. FEC/43/97]

²⁰ Interview with Ato Anteneh Girma, Manager of Credit Service Central Processing Unit at Commercial Bank of Ethiopia, on *the letter of credit operation in the Ethiopian Banking Practice*, 5 March, 2018

²¹ *Ibid*

suitable legal frameworks and appropriate practical operations. In view of this, the researcher identified it as an area of major importance that needs further study and investigation. The following problems, among others, are the major inquiry areas in the study.

To begin with, due to development of new forms and features of letter of credit in import and export business transactions the laws regulating letter of credit in Ethiopia faced a bunch of legal problems. The rules in the Commercial Code, and elsewhere, of the country on letter of credit have been criticized by the business community and academia for being incomplete and lagging behind modern developments.²² Occasionally, adequacy of the existing legal framework is questioned in the following areas:

- Its sufficiency for effectively regulate vital operations of letter of credit. The operation of letter of credit passes through different cycles of issuance, revocation, amendment, advice, confirmation, presentation of documents and payment during its life time. Thus, to what extent these essential stages of letter of credit regulated in Ethiopia is a matter that deserves an investigation.
- Its adequate incorporation of the principle of independence and fraud exception. The letter of credit law should be crafted in such a way that make the instrument independent from any contracts accompanying it, including the underlying contract concluded between the buyer and seller. Thus, the bank's obligation will be limited on dealing documents and not goods. However, with the growing use of letter of credit in Ethiopia, it has become an area for litigation over fraud. The fraudulent seller may forge documents to receive payment while it sends rubbish items or ships nothing at all. Therefore, a detail study is needed to identify the extent of recognition of the independent principle and fraud exception in the Ethiopia legal framework.
- Its adequate recognition and regulation of the principle of strict compliance in letter of credit operations. The principle basically denotes the fact that, documents presented by the beneficiary should be strictly conform to the terms and conditions of the credit and relevant legal rules. At this juncture, what endure the conditions for strict compliance and should every minor discrepancy considered as non-compliance are matters that needs analysis in lite of the Ethiopian legal framework.

²² Tilahun *et al*, *Position of the Business Community*, p.70

- Its proper regulation of parties to the letter of credit and their mutual undertakings. Letter of credit transaction needs the participation of different parties and there arises rights and obligations to one another. Therefore, adequacy of the Ethiopian legal framework on regulation of rights and obligations of the parties need to be examined.
- Lastly, capability of the Ethiopian legal framework towards regulating the electronic letter of credit operations that are emerging in the Ethiopian banking industry is a matter that needs an examination.

When we come to the banking practice of letter of credit operations in Ethiopia several problems are complained on daily basis. Documentary fraud, discrepant documents, restrictive time limits for compliance and so on are among the issues severally raised by the business community.²³ As practical operation is the backbone for vigorous functioning of the instrument in the market²⁴ a critical study is needed to figure out the problem and find out appropriate solutions.

Generally, despite vital importance of examining legal frameworks and practical operations of letter of credit in Ethiopia, legal scholars have given little, if not at all, attention to the issue. The aim to address this gap is the main driving forces behind researching in the subject matter.

1.3. Objectives of the Study

1.3.1. Central Objective of the Study

The central objective of the study is examining adequacy of letter of credit regulatory frameworks and practical challenges in Ethiopia.

1.3.2. Specific Objectives of the Study

- To scrutinize adequacy of Ethiopian laws regulating letter of credit transactions
- To apprise the banking practice and major challenges of letter of credit operations in Ethiopia
- To analyze existence of necessity for further reform of letter of credit operations and regulatory frameworks in Ethiopia and pinpoint the areas of reform, if any
- To identify what Ethiopia needs to learn from international experiences in this regard.

²³ Interview with Ato Gezu Ayele Mengstu, Banking law Legal Advisor and legal service Manager at Addis International Bank, on *the letter of credit operation and legal framework in Ethiopia*, March 4, 2018

²⁴ Magreth Otieno, *Analysis of the Law and Practice Governing Letter of Credit: Case Study of Selected Institutions in ILALA DAR ES SALAAM*, LL.M Dissertation, Mzumbe University, School of Law, 2013, p. 5 [Herein after Margreth, *Analysis of the Law and Practice Governing Letter of Credit*]

1.4. Research Question

1.4.1 Central Research Question

The central research question of the study is the following: is the current regulatory frameworks of letter of credit in Ethiopia adequate and what practical challenges are encountered its operation?

1.4.2. Specific Research Questions

- How far Ethiopia's regulatory framework of letter of credit adequate enough?
- What are the banking practice and major challenges of letter of credit operation in Ethiopia?
- Is there a need for further reform in the operation and regulation of letter of credit in Ethiopia and what should the reform be, if any?
- What can the country learn from international experiences in this regard?

1.5. Significances of the Study

Despite vital importance of letter of credit transactions in Ethiopia there is dearth of legal studies that examine its legal framework and practical operations. Hence, this study which focus on regulatory frameworks and practical operations of letter of credit transactions in Ethiopia will have the following importance.

- Enable drafters engaged in the ongoing revision of the Commercial Code to identify limitations of the exiting code on adequately regulating letter of credit issues
- It will raise awareness of judges, bankers, regulatory organs, legal practitioners, importers, exporters and academicians in the subject matter.
- It will incite other researchers to investigate more in the field
- Lastly, it will serve as an academic reference material

1.6. Scope of the Study

The study focuses on exploring operations and regulatory frameworks of letter of credit used for financing both in the import and export commercial transactions. Hence, it does not encompass payment guarantee mechanisms like stand by letter of credit. Geographically, the study is delimited to Federal Democratic Republic of Ethiopia.

1.7. Limitations of the Study

One of the major limitation that the writer encountered while conducting the study is lack of relevant materials in relation to regulatory frameworks and practical operations of letter of credit in Ethiopia. Besides, time constraint and reluctance of private banks and businesspersons to disclose information

relating to their letter of credit are also another limitations that the researcher faced in the study. With great endeavor, the researcher avoided the impact of such limitations on the quality of the study.

1.8. Methodology of the Study

1.8.1. Design of the Study

For properly addressing the research questions framed, the objectives set and for its quality of being the best research tool for in-depth study, with high degree of flexibility²⁵, of polices, laws, theories and principles regulating letter of credit and its practical operations in Ethiopia, the researcher employed qualitative research methodology. Under the ambit of qualitative research both doctrinal and empirical methods were employed.

Doctrinal legal research method had been used to analyze statutory provisions, court cases, principles and doctrines through the power of reasoning. Besides, the researcher discussed the Ethiopian law and practice mainly along with the latest version of Uniform Customs and Practice for Documentary Credits (UCP600) and Uniform Commercial Code of America (herein after referred UCC). The UCP600 is opted for the reason that the instrument is one of the leading international rule that is developed from customs of documentary credits²⁶ and accepted by almost all banks around the world.²⁷The UCC, on the other hand, is selected as it is a well-crafted legislative enactment of contemporary letter of credit practices that combine both technical and legal concepts of letter of credit.²⁸Empirical legal research method had been also employed through personal interview with various stakeholders to find out problems of letter of credit operations in Ethiopia. By employing both of these research methods together, the researcher acquired the advantage of rectifying the weakness of one of the method by the other.

1.8.2. Participants of the Study and Sampling Technique

As the position, experience, expertise and other qualifications are vital for properly addressing research questions of the study the researcher employed purposive sampling to determine

²⁵ Mike McConville and Wing Hong Chui, *Research Methods for Law*, Edinburgh University Press, Scotland, 2007, p. 49

²⁶ Zsuzsanna, *Documentary Credits in International Commercial Transactions*, p. i

²⁷ Hamed Alavi, 'Documentary Letters of Credit, Legal Nature and Sources of Law' *Journal of Legal Studies*, 2016, Vol. 16, Issue 31, pp. 106-121, at 112 [Herein after Hamid, *Documentary Letters of Credit*]

²⁸ Boris Kozolchyk, 'Legal Aspects of Letters of Credit and Related Secured Transactions', *Lawyer of the Americas*, 1979, Vol. 11, No. 2/3, pp. 265-284, at p. 270 [Herein after Boris, *Legal Aspect of Letter of Credit*]

participants of the study. In order to satisfy specific needs in the research Commercial Bank of Ethiopia, Hibret Bank Share Company, Development Bank, Addis International Bank, Wegagen Bank and Oromiya International Bank are selected among commercial banks operating letter of credit in Ethiopia. Besides, the researcher selected key informants from National Banks of Ethiopia and selected expertise in the field through purposive sampling.

Due to the nature of the research and the methods employed, qualitative method, the data were collected from the participants until the usual criterion of redundancy or data saturation is met.

1.8.3. Data Sources and Collection Tools

The researcher used both primary and secondary data. Primary data was collected from participants of the study through semi-structured interview. Semi-structured interview is selected for its quality of enabling the researcher formal communications with possible flexibilities in order to probe for views and opinions of the interviewee. On the other hand, Secondary data were gathered, among other things, from polices, laws, court cases, books, journals, working papers, magazines, newspapers and internet sources.

1.8.4. Data Analysis Technique

Primary and secondary data collected through various data collection tools had been analyzed by qualitative data analysis techniques of descriptive and analytical methods. Hence, the researcher first prepared the data into analyzable form. It includes, but not limited to, making commentaries on different legislations, translating documents written in other languages than English and arrange documents in order of their relevancy. Secondly, the researcher closely examined the data and made familiarity with them. Thirdly, the data was arranged for final interpretation. That includes code or index the data in the form of names, initials or numbers. Then different themes were identified and the relationship in each category was studied. Fourthly, concepts which enable to reach on a certain generalized statement were developed. Finally, the researcher verified validity of the data through triangulation of research methods and data collection tools.

1.9. Over view of chapters

For properly address the objectives set and main questions forwarded the paper is composed of five chapters. The first chapter address introduction of the study that comprises of background of the study, statement of the problems, objective of the study, research questions of the study,

significance of the study, review of literature, scope of the study, limitations of the study, methodology of the study and overview of chapters.

The second chapter provide the general overview of letter of credit. It focus on general concept and definition of letter of credit, parties to a letter of credit, historical origin of letter of credit, classification of letter of credit, functions of letter of credit, sources of letter of credit law and finally legal scope of the ICC letter of credit rules.

The third chapter of the study deals the adequacy of letter of credit regulations in Ethiopia. In this part of the study, the researcher explored regulation of vital operations of letter of credit transactions, the doctrine of autonomy of letters of credit and fraud exception, the doctrine of strict compliance, the parties to the letter of credit and their mutual undertakings and lastly, electronic letter of credit under the Ethiopian legal framework.

The fourth chapter investigates banking practice and major challenges of letter of credit operations in Ethiopia. Finally, the last chapter provides conclusion and recommendations.

CHAPTER TWO

GENERAL OVERVIEW OF LETTER OF CREDIT

2.1. General Concept and Definition of Letter of Credit

Letter of credit is generally understood as an arrangement in which the issuing bank, at the request and in accordance with the instruction of the applicant, undertakes to pay a beneficiary or reimburse the paying bank against presentation of documents and satisfactory compliance with the terms and conditions stipulated therein. It is a legal instrument which binds all parties and mainly issued to facilitate the payment for goods in import and export transactions.²⁹

One of the confusing elements of any discussion on letter of credit is the blizzard of different interchangeable terminologies employed by various literatures and legal documents.³⁰

Documentary credit, documentary letter of credit, letter of credit, commercial letter of credit, banker's commercial credit and credit are some of the nomenclatures employed in different literatures. Common law countries usually used the term "documentary credits", or "banker's commercial credits".³¹The UCP600 uses the term documentary credit and credit interchangeably.³²

The Commercial Code of Ethiopia prefer the terminology "documentary credit"³³ while in the Ethiopian banking practice it is widely recognized as "letter of credit" or as "L/C".

It is also difficult to come up with a single and precise definition for the term letter of credit. Such a difficulty is triggered by existence of different functions of letter of credit conceived by the commercial communities³⁴ and the difference on various parties, documents and actions that make up letter of credit law and practice across jurisdictions. This has resulted formulation of different definitions for the instrument. Hence, a look at some of these definitions will help to develop a comprehensive understanding of the instrument.

William E. McCurdy define letter of credit as

²⁹ Nicholas L. Deak, 'Letters of Credit (Documentary Credit)', *N.Y.J. Int'l & Comp. L.*, 1981, Vol. II, pp. 229-252, at p. 239 [Herein after Nicholas, *Letter of Credit*]

³⁰ Garth C. Wooller, *Legal and Practice Perspectives on Documentary Credit under the UCP600*, Brisbane, Australia, 2007, p. 9 [Herein After Garth, *Legal and Practice perspective on Documentary Credit*]

³¹ Zsuzsanna, *Documentary Credits in International Commercial Transactions*, p. 18

³² The Uniform Customs and Practice for Documentary Credits, 2007 Revision, ICC Publication no. 600 ("UCP"), Article 1 [Herein After UCP600]

³³ Commercial Code of the Empire of Ethiopia, 1960, *Negarit Gazeta*, Extraordinary issue, Proclamation No.166 of 1960, 19th year. No. 3, Book IV, Title III, Chapter 5, of Section 4 [Herein after the Commercial Code of Ethiopia]

³⁴ Susmitha P Mallaya, *Documentary Credit Law: An Indian Perspective*, PHD Dissertation, Cochin University of Science and Technology, School of Legal Studies, 2007, p. 4 [Herein after Susmitha, *Documentary Credit Law*]

Any letter whereby the writer authorizes some other person to draw bills of exchange on the writer or upon some designated third person and undertakes either expressly or by implication that drafts drawn in compliance with the terms of the letter will be accepted and paid.³⁵

The writer defines the term from the very narrow view point of letter of credit. According to this definition certain transaction will be characterized as letter of credit if it relates with payment only. The reality is, however, there are different kinds of letter of credit other than payment letter of credit. To name a few; negotiation credit, transferable credit, back-to-back credit, acceptance credit and so on.

Professor Kozolchyk defines letter of credit as “a mercantile currency embodying an abstract promise of payment, which possesses a high, though not total, immunity from attack on the ground of breach of duty of the seller to the buyer.”³⁶ The definition tried to make an emphasis on the independent nature of letter of credit. However, it failed to describe the parties to the letter of credit and their respective roles. It also overlook other basic features and functions of letter of credit.

Another scholar named Davis³⁷ tried to come up with a descriptive kind of definition. According to him letter of credit is;

A letter whereby one person (usually a merchant or banker) promises another person (who is either named in the letter, or to whom it is intended that the letter shall be shown and who is known as the “beneficiary”) that he will reimburse the beneficiary any amounts for which he may give credit to a third person (usually a customer of the person giving the letter), either by the shipment of goods or payment of money, in respect of a commercial transaction into which the beneficiary has entered or intends to enter with the third party.

This definition is also incomplete. For instance, it does not show the nature of letter of credit and the documents that shall be submitted by the beneficiary in order to get payed by the authorized bank.

Black’s Law Dictionary define the term as;

An instrument under which the issuer (usu. a bank), at a customer's request, agrees to honor a draft or other demand for payment made by a third party (the beneficiary), as long as the draft or demand

³⁵ William E. McCurdy, ‘Commercial Letter of Credit’, *Harvard Law Review*, 1922, Vol. 35, No. 5 , pp. 539-592, at p. 543 [Herein after William, *Commercial Letter of Credit*]

³⁶ “Advising And Verification Of Letter Of Credit Law Commercial Essay” at <<https://www.uniassignment.com/essay-samples/law/advising-and-verification-of-letter-of-credit-law-commercial-essay.php#ftn98>> [Last accessed 5 April, 2018]

³⁷ A. G. Davis, *The Law Relating to Commercial Letters of Credit*, Sir Isaac Pitman & Sons Ltd., London, 1963, p. I [Herein after Davis, *The Law Relating to Commercial Letters of Credit*]

complies with specified conditions, and regardless of whether any underlying agreement between the customer and the beneficiary is satisfied.³⁸

The definition tries to address the parties involved in the letter of credit and the respective responsibilities, the independent nature of the transaction from the underlying contract and the beneficiary's duty to fulfill the conditions specified therein.

In article 2 of UCP600, letter of credit is any arrangement that is irrevocable whereby a bank (the "issuing bank") acting at the request and on the instructions of a customer (the "applicant") to honor a complying presentation (by the "beneficiary") in accordance with the terms and conditions of the credit, the applicable laws and international standard banking practice. Once the conditions under credit is satisfied the issuing bank will be under obligation to make a payment to or the order of the beneficiary. However, this definition is still unsatisfactory. It excludes the revocable letter of credit from the ambit of letter of credit, thereby, restrict the choice of the parties to have their own choice of letter of credit types.³⁹

When we come to Ethiopia, the Commercial Code under article 959 renamed the document as documentary credit and defines it as "... a credit opened by a bank providing for payment against presentation of specified documents to the opening bank or to its agent." The definition is short of essential features of letter of credit. Several decisive issues of letter of credit such as, at whose request and to whose benefit letter of credit is opened? How the bank can effect payment to the beneficiary? What is the obligation of the issuing (opening) bank? Extent of responsibility of corresponding banks? And so on are left untouched.

Some lawyers and bankers in Ethiopia confused documentary letter of credit with that of standby letter of credit. However, these two commercial instruments are verily different, thus, they should be distinguished.

Standby Letter of Credit, unlike letter of credit, is a payment or performance guarantee used in the import and export transactions. It is made to substitute the bank guarantee in the transaction than used for payment modality. It often referred as nonperforming letter of credit since it only used as a guarantee when the buyer failed to pay as indicated in the contract.⁴⁰ It can be required from both importers and exporters. When trade across borders are get bigger and complicated, basically after

³⁸ *Black's Law Dictionary*, 8th ed., s. v. "letter of credit"

³⁹ Susmitha, *Documentary credit Law*, p. 9

⁴⁰ Ron Borcky, "*Understanding and Using Letters of Credit Part II*", at <<https://www.crfonline.org/orc/cro/cro-9-2.html>> [Last accessed 8 May, 2018] [Herein after Ron Borcky, *Understanding and Using Letter of Credit*]

WWII, the importers needed a guarantee from their suppliers that the latter will deliver the product for which the payment is already effected. The exports in turn needs a guarantee from the importer that he/she will effect payment in line with their contractual agreements. In response to this need of the commercial community, the American and European Banks develop standby letter of credit.⁴¹

In general, unlike letter of credit, standby letter of credit cannot serve as payment instrument for import and export transactions rather it is an instrument that enables the buyer to establish a relationship with the seller by showing its commitment of payment guarantee. Currently it can be issued to guarantee repayment of loans, to ensure fulfillment of a contract, to assure payment of the purchase price of goods and alike transactions.⁴²

2.2. Parties to a Letter of Credit

There are four contractual parties under letter of credit transactions. These are the applicant, beneficiary, issuing bank and corresponding bank.

The applicant is a party who instruct the credit to be issued.⁴³ The applicant is usually the buyer in the international trade. A prospective buyer who wants to buy goods from a prospective seller in another locality usually opens letter of credit to effect purchase price of the products while avoiding the risk of paying the entire purchase price without knowing the seller is complying, at least in terms of evidentiary document, with the underlying sale contract between them.

The beneficiary is a party in whose favor a credit is issued.⁴⁴ In the international trade the seller is usually the beneficiary of letter of credit. The seller who manufactures the product or buy the merchandise from another producer wants to make sure that the buyer will take the products and pay the purchases price up on production, procurement or transportation of the products.⁴⁵ Hence, he may require the applicant to open of letter of credit in favor of him. Accordingly, the seller will be the creditor of the applicant upon complying with the credit, hence, he will be beneficiary of the credit.

The issuing bank is a bank that issues a credit at the request of an applicant or on its own behalf.⁴⁶It usually referred as the buyer's bank. It opens letter of credit at the instruction of the buyer and

⁴¹ Susmitha, *Documentary Credit Law*, p. 23

⁴² Ron Borcky, *Understanding and Using Letter of Credit*

⁴³ UCP600, Article 2

⁴⁴ Ibid

⁴⁵ William, *Commercial Letter of Credit*, p. 540

⁴⁶ ÜCP600, Article 2

undertakes to honor a draft or other demand for payment made by the beneficiary or to his order. It will operate the letter of credit with strict compliance of terms and conditions detailed in the credit. Involvement of the issuing bank is one of the decisive factor for letter of credit transactions. The issuing bank is required to perform all activities assigned to it under the credit and relevant laws with due care and diligence.

Corresponding bank is the other parties in the letter of credit operation. The seller in the international trade may not rely only in the creditworthiness of the seller's bank (issuing bank) and it might also be difficult for the issuing bank to operate lonely the credit transacted abroad, hence, a corresponding bank in the locality of the buyer needed. The Corresponding bank may serve as advising bank or conforming bank. Advising bank undertakes to authenticate the letter of credit and the documents submitted by the beneficiary. Its obligation is limited to advice the credit, hence, it does not have any responsibility to pay the beneficiary irrespective of the obligation of the issuing bank.⁴⁷ Conforming bank, on the other hand, is a bank that adds its confirmation to a credit upon the authorization or request of the issuing bank.⁴⁸ Any bank still can be conforming bank at its initiation or at the request of the beneficiary. The conforming bank will have an obligation equivalent to the issuing bank. It is obliged to honor a draft or other demand for payment made by the beneficiary as far as the terms and conditions under the credit are satisfied.

There are at least three separate pertinent contractual relationships between the applicant, beneficiary, issuing bank and corresponding bank that arise within letter of credit transactions. The first one is, the sale contract between the buyer and the seller which commonly referred as the underlying contract.⁴⁹ The second one is, a contract between the buyer and the issuing bank that the buyer instructs for the opening of letter of credit. Third, a contract between the issuing bank and the beneficiary (usually the seller) that the latter will be paid the purchase price stated in the credit subject to the duty to submit the required documents dully and effectively. Apart from these, there might be a fourth contract between the issuing bank and correspondent bank in which the latter serve as advising or conforming bank. It will entrust to advise and/or confirm the credit,

⁴⁷ Vasile Nemes, 'Documentary Letter of Credit in the Regulation of 600-Paris Publication', p. 221 at <http://webcache.googleusercontent.com/search?q=cache:3HpgFt8aeQJ:cks.univnt.ro/uploads/cks_2011_articles/index.php%3Fdir%3D01_law%252F%26download%3Dcks_2011_law_art_024.pdf+&cd=1&hl=en&ct=clnk&gl=et> [Last accessed 8 May, 2018]

⁴⁸ UCP600, Article 2

⁴⁹ Chumah Amaefule, *The Exceptions to the Principle of Autonomy of Documentary Credits*, PHD Dissertation, University of Birmingham, School of Law, 2011, p. 14 [Herein after Chumah Amaefule, *The Exceptions to the Principle of Autonomy of Documentary Credits*]

collection of documents and payment on acceptance or negotiation up on fulfillment of terms and conditions specified under the credit.⁵⁰

2.3. Historical Origin of Letter of Credit

As some scholars argue, the origin of letter of credit is traced back to ancient Egypt and Babylon.⁵¹ Some writers mention the use of letter of credit in the Ancient Egypt in 248 B.C and in Babylon in the 3000 B.C.⁵² Researchers also confirmed that Banks' of Ancient Greece were used letter of credit in commercial transactions to ease the difficulties relating to transportation of specie.⁵³ The collapse of Roman Empire significantly reduce trade across Empires and, consequently, reduce use of commercial letter of credit. The re-establishment of European Cities in the 12th and 13th century marked the reinstatement of letter of credit usage in the commerce. It was employed to avoid the risk of robbery and to alleviate the shortage of trade currency.⁵⁴ Zsuzsanna Tóth also mentioned the use of letter of credit in Italy during the 14th and 15th Century which is almost similar to the letter of credit employed by the commercial community today.

The various provisions of the letters are strikingly similar to those of the modern letters of credit. They stated for example that (a) payments are to be made as requested by a named beneficiary; (b) the payments could not exceed a specific sum; (c) the payor shall obtain receipts from the beneficiary; (d) the payment shall be charged to the account of the issuer with the payor; or (e) upon receipt of a written notice from the payor that the amount has been paid, the issuer shall credit the payor's account accordingly.⁵⁵

In the 17th century, letter of credit become prevalent financial instrument in United Kingdom and other parts of Europe.⁵⁶ Latter in the 19th century, British banks gained monopoly over issuance of letter of credit due to acceptance of Pound Sterling in the international trade of that time.⁵⁷ Dominancy of British Banks in letter of credit operation continued until WWI. However, the

⁵⁰ Ibid

⁵¹ Zsuzsanna, *Documentary Credits in International Commercial Transactions*, p. 1

⁵² Zsuzsanna, *Documentary Credits in International Commercial Transactions*, p. 1

⁵³ Frank Roland Hans Mueller, *Letters of Credit with Focus on the UCP 600 and the Exceptions to the Principle of Autonomy with Emphasis on the "Fraud Rule" Under The Laws of the USA, the UK and the RSA*, Mini Thesis, University of the Western Cape, School of Law, 2013, p.2 [Herein after Frank, *Letters of Credit with Focus on the UCP 600*]

⁵⁴ Ibid

⁵⁵ Zsuzsanna, *Documentary Credits in International Commercial Transactions*, p. 2

⁵⁶ Frank, *Letters of Credit with Focus on the UCP 600*, p.2

⁵⁷ Ibid

outbreak of WWI changed the situation that causes the British lost part of its domination in the international trade to United States of America (USA).⁵⁸

After WWII, America emerged as the world leading actor of the international trade. It became the most important supplier and the larger importer of goods in the world. As a result, operation of letter of credit for import and export transaction boom to the extent ever imagined in that country.⁵⁹ In subsequent centuries, use of letter of credit become widespread across all parts of the world.⁶⁰ In Ethiopia, there is no record that shows where exactly letter of credit is employed in its commercial transactions. Conceptually, it was began in 1905 with the introduction of modern banking up on establishment of the Abyssinia Bank. The bank was established in 1905 based on the agreement between the Ethiopian Government and the National Bank of Egypt (that was owned and managed by United Kingdom).⁶¹ The bank was engaged in commercial banking services such as selling shares, accepting deposits and effecting payments in a cheque, issue currency notes,⁶² finance international trade and the like.⁶³ As the bank is established by the bank owned and managed by England, it adopts most of the instruments operated therein that includes letter of credit.⁶⁴ The instrument which was unknown to the then traders, however, was not as such practically employed. Its application in the import and export transactions was grew in 1990s following the country's re-introduction of market led economic policy.⁶⁵ Despite its chopped history, it becomes the most important instrument in today's import and export transactions of Ethiopia.

2.4. Types of letter of credit

In earlier times there were only two types of letter of credit, namely, revocable letter of credit and irrevocable letter of credit. When the needs of traders in the import and export transactions increased banks specialize their letter of credit and craft different kinds of the document with

⁵⁸ Nicholas, *Letter of Credit*, p. 230

⁵⁹ Ibid

⁶⁰ Frank, *Letters of Credit with Focus on the UCP 600*, p.2

⁶¹ Arnaldo Maur, 'The Short Life of the Bank of Ethiopia', *ECONOMICA*, 2014, p. 105 at <<http://www.researchgate.net/publication/228466309>> [Last accessed 3 April 2018] [Herein after Arnaldo, The short life of the Bank of Ethiopia]

⁶² Fasil Alemayehu and Merhatbeb Teklemedhin, *Law of Banking, Negotiable Instruments and Insurance Teaching Material*, Justice and Legal System Research Institute, 2009, p. 9

⁶³ Arnaldo, *The short life of the Bank of Ethiopia*, p. 107

⁶⁴ Interview with Mesfin Getachew, Chief Legal Expert at National Bank of Ethiopia, on *historical background of letter of credit in Ethiopia*, 6 March, 2018

⁶⁵ Ibid

distinct features and legal consequences.⁶⁶ The ingenuity of the commercial community in this regard is taken as one of their terrific contribution towards the international business.⁶⁷ Now a days there are different varieties of letter of credit used in the import and export transactions. The following is a brief description of some special letters of credit.

2.4.1. Clean and Documentary Letter of Credit

The classification on clean and documentary letter of credit is based on the need for documentation to comply with the requirements of the credit. Accordingly, the credit will be characterized as clean when it does not require documentation for acceptance or negotiation of a draft. On the other hand, the credit will be recognized as documentary when payment or negotiation of a draft conditioned with provision of accompanying documents such as shipping document, insurance document, invoice and the like by the beneficiary. Despite this classification, it is Documentary Letter of Credit that used by the commercial community most.⁶⁸

2.4.2. Revocable and Irrevocable Letter of Credit

Revocable letter of credit is one variety of the credit that gives a greater flexibility for the applicant to modify or cancel the credit without the consent and even prior notice to the beneficiary.⁶⁹ The bank is not also liable for the revocation of the credit and nor obliged to notify any of the modification. In *Cape Asbestos v. Lloyd's Bank*⁷⁰, the court decided that, the banker is under no obligation to notify the beneficiary cancellation of revocable letter of credit. This is applicable despite the usual practice of bankers notifying the beneficiary in their previous relations.⁷¹

An irrevocable letter of credit constitutes an absolute undertaking by the issuing bank to pay and accept drafts and/or documents drawn by the seller provided that the latter presents the documents as required at the indicated time. It gives greater assurance to the beneficiary that the payment by the banker cannot be cancelled or modified.⁷² The seller has a right against the banker to get payed irrespective of the underlying contract.⁷³ The buyer cannot cancel or modify the terms of the irrevocable credit without an express consent of the beneficiary. Nor the banker can change the

⁶⁶ Susmitha, *Documentary Credit Law*, p. 13

⁶⁷ Davis, *The Law Relating to Commercial Letters of Credit*, p. I

⁶⁸ William, *Commercial Letter of Credit*, p. 544

⁶⁹ Zsuzsanna, *Documentary Credit in International Commercial Transactions*, p. 23

⁷⁰ *Cape Asbestos Co v. Lloyd's Bank* [1921] W.N. 274

⁷¹ Susmitha, *Documentary Credit Law*, p. 14

⁷² Zsuzsanna, *Documentary Credit in International Commercial Transactions*, P. 22

⁷³ Reinhard Langerich, *Documentary credits in practice*, 2nd edi., From & Co, Glostrup, Denmark, 2009, p. 83 [Herein after, Reinhard, *Documentary Credits in Practice*]

terms or cancel the credit even if the buyer has gone bankrupt or unable to comply with the credit for other reasons. Thus, any change or modification of the irrevocable letter of credit should be at the request of the buyer and clear agreement of the beneficiary. This makes irrevocable credit the most accepted method of payment in the international trade.

2.4.3. Conformed and Unconfirmed Letter of Credits

The classification of conformed and unformed credit is stand from the undertaking of the corresponding bank. Confirmation refers the fact that the corresponding bank take the undertaking that it will pay or accept drawings from the beneficiary provided that terms and conditions under the credit are met.⁷⁴

The beneficiary will have a steady undertaking of another bank in addition to the opening bank. It is to the best advantage of the beneficiary that he gets a banker at his location which its reputation and liquidity known to him. Cost of adherence to the terms and conditions of the credit will significantly reduce when the banker is existed in the seller's location than somewhere else abroad. It is also true that, the bankers risk will be localized, thus, any settlement with local bank is far better than the issuing bank which found across borders. However, such kind of letter of credit is costlier to the parties, since the conforming bank will obviously charges for its service.⁷⁵ It shall be noted that, confirmation can be added only on irrevocable letter of credit.⁷⁶ Thus, no confirmation can be added for revocable letter of credit. The main reason is that, revocable letter of credit cannot go together with the very nature of conformed letter of credit since the latter necessitates an absolute undertaking by the conforming bank to pay the beneficiary irrespective of its relationship with the issuing bank or the applicant.

Unconfirmed letter of credit on the other hand is a credit which its payment is not guaranteed by any bank other than the issuing bank.⁷⁷ The responsibility of seller's bank is limited to merely checking the apparent authenticity of the credit and inform the beneficiary without assuming any responsibility towards the latter.⁷⁸ It is less secure mode of letter of credit compared to the conformed one.

⁷⁴ Susmitha, *Documentary Credit Law*, p. 19

⁷⁵ Union Bank of India, types of LC (Chapter 20), p. 10, at <<https://www.unionbankofindia.com>> [Last accessed at 14 April 2018] [Herein after Union Bank of India, *Types of LC*]

⁷⁶ Union Bank of India, *Types of LC*, p. 5

⁷⁷ Nasdaq, *Unconfirmed Letter of Credit*, at <<https://www.nasdaq.com/investing/glossary/u/unconfirmed-letter-of-credit>> [Last accessed at 14 April, 2018]

⁷⁸ Zsuzsanna, *Documentary Credits in International Commercial Transactions*, P. 24

2.4.4. Transferable Letter of Credit

It is a type of letter of credit that allows the seller (the original beneficiary) to transfer all or part of the proceeds of the original letter of credit to one or more beneficiaries, secondary beneficiary.⁷⁹ when the seller is not actually manufactured the products to be supplied, the buyer may issue a credit which allowed the seller to open and instruct the correspondent bank to transfer it to some other beneficiary who actually manufacture and supply the product to the beneficiary. Thus, the role of the seller is just like a middleman or dealer.⁸⁰ Letter of credit can be transferable if and only if a statement to that effect is clearly specified therein and the secondary beneficiary cannot transfer it to some other persons.⁸¹ This kind of letter of credit usually used by the seller to avoid any direct dealing between the buyer and the supplier so that the middleman (seller) will earn his portion from the transaction between the two parties.⁸²

2.4.5. Back-to-Back Letter of Credit

Back to back letter of credit is used when the actual supplier of the product is not the seller himself, but some other person and the original letter of credit is not made transferable to third person suppliers. At this juncture, the seller will open letter of credit to the supplier with a guarantee of the original letter of credit called back-to-back letter of credit.⁸³The original letter of credit will be used as a collateral for the second letter of credit issued by the seller.⁸⁴

2.4.6. Deferred Payment Letter of Credit

Deferred Payment Letters of Credit, sometimes called Usance Letter of Credit, is another variety of letter of credit that provides a sort of flexibility to the buyer. It is an arrangement in the credit that the buyer will not be obliged to pay the issuing bank immediately when it receive the complying documents. The seller will be required to wait the maturity of payment date specified under the credit after shipment of the products. It gives the buyer a fixed time as a grace period for payment. This period can be used by the buyer to resell the products and use the earnings for the payment. However, the seller might be comparatively disadvantaged if he needs the immediate payment of the purchase price.⁸⁵

⁷⁹ Union Bank of India, *Types of LC*, p. 5

⁸⁰ Ibid

⁸¹ Ibid

⁸² Zsuzsanna, *Documentary Credits in International Commercial Transactions*, p. 27

⁸³ Id, p. 28

⁸⁴ Susmitha, *Documentary Credit Law*, p. 22

⁸⁵ Id, P. 21

2.4.7. Red Clause and Green Clause Letter of Credit

Such kind of letter of credit enables the beneficiary to receive advance payments from the corresponding bank before effecting shipment of the products to the buyer. It derives its name from the fact that its terms are usually written and printed in red-ink.⁸⁶The corresponding bank will provide the pre-shipment credit to the beneficiary as indicated in the credit. The seller will have such opportunity having extra fund for financing its production process. However, it is more risker to the buyer. Because, if the seller fails to export the goods or failed to repay the advance it will be to the entire risk of the buyer. The recourse right of the corresponding bank against the issuing bank and the right of the issuing bank against the buyer will not be affected.

Green Clause letter of credit, on the other hand, is an extension and refinement of the Red Clause Letter of Credit⁸⁷, in that the seller can receive advance payments from the corresponding bank provided that the former put the goods in warehouse for shipment and adduce warehouse receipt to that effect.⁸⁸ Thus, the banker will give him the advance payments by tacking the warehouse receipt as documentary evidence

2.4.8. Revolving Letter of Credit

A Revolving Letter of Credit is commonly used by the buyer to finance transactions made with his frequent customer. It also employed to finance import transactions made via installment for a certain period of interims.⁸⁹ In such a transaction, the amount in the credit is renewed or reinstated periodically without renewing the terms and conditions specified therein.⁹⁰ However, the maximum drawings by the seller and restoration by the banker might be limited to a certain numbers by the credit or legal rules.⁹¹

2.4.9. Sight Payment and Acceptance letter of credit

The classification of sight payment and acceptance letter of credit is based on the time of payment and existence of a need to present a draft. The credit will be considered as sight when the credit is designed in such a way that the beneficiary will be paid at the time he demands provided that terms and conditions in the credit and relevant laws are satisfied. On the other hand, the credit will be

⁸⁶ Id, p. 24

⁸⁷ Zsuzsanna, *Documentary Credits in International Commercial Transactions* p. 27

⁸⁸ Union Bank of India, *Types of LC*, p. 7

⁸⁹ Susmitha, *Documentary Credit Law*, p. 23

⁹⁰ Union Bank of India, *Types of LC*, p. 4

⁹¹ Id, p. 5

considered as acceptance where the payment for the beneficiary in the future time. Thus, the beneficiary needs to submit a draft to the issuing bank for future payment.

2.5. Functions of letter of credit

Buyers and sellers engaging in international business transactions are often separated by thousands of miles, special precautions are often taken to ensure performance under the contract. Either the exporter or the importer may not trust its respective partner abroad, hence, each party targets to protect its individual interests. The seller wants to avoid delivering goods for which they might not be paid. The Buyer, on the other hand, desires the assurance that seller will not be paid until there is an evidence that the required goods have been shipped.⁹² Existence of risks in the international trade makes the credit arrangement between the buyer and the seller as important as the quality, quantity, price and delivery of the product.⁹³ The letter of credit that are frequently used to facilitate international business transactions are supposed to have the following functions

2.5.1. Seller's security for payment

The international trade exposes the seller (exporter) to various substantial risks. The seller will always eager to get paid purchase price of every single products at the earlier possible opportunity. However, this very needs of the seller will face several risks inherent in the international commerce. The payment for the seller might be impeded by the risks resulting from long distance between the contracting parties, lack of information about solvency of the parties, divergent law and business practices, different currencies, difficult communication systems, difficulties to access information of other countries, existence of different political systems, transportation difficulties, and erratic state related risks of war, rebellion, revolution, confiscation and expropriation.⁹⁴ The introduction of letter of credit mitigate these risks and enable the seller to get payed irrespective of the problem of the buyer or the political condition in the latter's country.

2.5.2. Liquidity and cash flow

The letter of credit not only assures payment to the seller, it also assures payment of the price at the exact time specified in the credit. Payment in the exact time as planned not only preserve time value of the money and avoid significant losses of interest but also it will ensure a predictable

⁹² Daniel C.K. Chow & Thomas J. Schoenbaum, *International Business Transactions, Problems, Cases and Materials*, Aspen Publisher, Austin, 2005, p. 61

⁹³ Boris Kozolchyk, *Commercial Letters of Credit in the Americas: A Comparative Study of Contemporary Commercial Transactions*, Bender, New York, 1966, p. 34

⁹⁴ Andreas, *Letters of Credit and the Doctrine of Strict Compliance*, pp. 12-13

pattern of incoming payments and give opportunities for companies to enter into financial arrangements.⁹⁵

2.5.3. The Buyer's Security and Cash Discount

A look at many of the significances of letter of credit, it is more of a “seller's document” and advantageous to the seller than the buyer.⁹⁶ But still we can see some of the advantages of letter of credit in terms of providing security to the buyer. The seller is firmly required to submit documents which shows the quality, quantity, price, production, packaging, shipment, insurance of the products as per the terms and conditions of the credit. Hence, the buyer can ensure correctness of the goods based on the contents of these documents submitted by the seller.⁹⁷ The problems related to forgery of documents can be mitigated through fraud exception rules and arrangement of inspection firms that inspects the goods are in accordance with the requirements of the importer.⁹⁸ Letter of credit also give a cash discount possibility to the buyer. As letter of credit is now become the most secured and preferred way of payment the buyer can take the cash flow advantage of the seller to get some discount from the purchase price of the products.

2.5.4. Instrument for finance

The other good thing with the use of letter of credit is, it serve as instrument of finance. Once the buyer opened a valid letter of credit what is expected from the seller is presentation of the documents as indicated in the credit and receive the payment at maturity. It is important method of payment as good as cash. It avoids any carriage of huge amount of money across national boundaries. The time, mode and currency of the payment can be flexibly arranged by the agreement of the parties.

2.5.5. Pre-export Finance

The seller might need a finance to facilitate the production of goods to be exported for the buyer under the letter of credit. In this instance, letter of credit provides two pre-export financing opportunities. The first one is, negotiate with the buyer for the issuance of Red Clause Letter of Credit. Then the said credit would let him to receive advance payments from the corresponding

⁹⁵ Reinhard, *Documentary Credit in Practice*, p. 36

⁹⁶ Id, p. 37

⁹⁷ Rosmawani Che Hashim *et al*, 'Principle of Autonomy in Letter of Credit: Malaysian Practice', *IIUM LAW JOURNAL*, 2011, VOL. 19 No. 2, pp. 202-242, at p. 210 [Herein after Rosmawani *et al*, *Principle of Autonomy in Letter of Credit*]

⁹⁸ Ch'ng, *International Trends in Documentary Credit Transactions*, p. 195

bank before effecting shipment of the products to the buyer. Second, the seller might request a pre-export finance or advance payments from his bank directly. Then the bank, based on the trust in the seller, may grant him the finance against security in the letter of credit.⁹⁹ However, it is important to note that letter of credit does not have actual value per se. Its value presupposes presentation of complying documents as required under the credit.¹⁰⁰

2.5.6. Regulatory Tool

Almost all countries in the world have their own monetary policies. They highly regulate in and out of the currency across their borders. Utilization of letter of credit for import and export transactions enable the government to easily regulate its currency. For instance, in Ethiopia money laundering is strictly prohibited and a legislation is enacted to suppress anyone who might engage in such activities.¹⁰¹ However, the proclamation by itself is not sufficient to tackle the problem, thus other mechanisms are devised. The primary of them is, prohibition of any purchases more than USD 5,000 (Five Thousand) except through letter of credit or Cash against Document.¹⁰² Besides, foreign exchange approval for import and export payment shall only be on the basis of letter of credit.¹⁰³ So that, NBE can easily regulate cash flow in the import and export transactions. Alike regulations also can be found in various jurisdictions.

2.6. Sources of Letter of Credit Law

Despite the long ago mercantile history of letter of credit transactions, the laws governing letter of credit introduced in much shorter times.¹⁰⁴ In the course of history letter of credit laws developed mainly from the customs of importers, exporters, bankers, insurance companies, shipping and freight forwarders.¹⁰⁵ Latter on the International Chamber of Commerce (herein after ICC) take the initiative and codified these customs and usages in a unified code called, Uniform Customs and Practice for Documentary Credits. Besides, ICC also codified several letter of credit rules such as; Uniform Customs and Practice for Documentary Credits for Electronic Presentation

⁹⁹ Reinhard, *Documentary Credit in Practice*, p. 38

¹⁰⁰ Ibid

¹⁰¹ Prevention and Suppression of Money Laundering and Financing of Terrorism Proclamation, 2013, *Federal Negarit Gazette*, Proc. No.780, 19th Year, No. 25

¹⁰² Directive No. FXD/07/1998, Article 5.4 cum 5.3 and 5.1

¹⁰³ Directive No. FEC/43/97, article 2.1

¹⁰⁴ Frank, *Letters of Credit with Focus on the UCP 600*, p.3

¹⁰⁵ Zsuzsanna, *Documentary Credits in International Commercial Transactions*, p. i

(eUCP), International Standard Banking Practice (ISBP) and Uniform Rules for Bank-to-Bank Reimbursements under Documentary Credits (URR).¹⁰⁶

2.6.1. The Uniform Customs and Practice for Documentary Credits

UCP is the product of harmonization process of international laws in order to facilitate international trade and reduce conflicts, thereby, create uniform letter of credit laws among different jurisdictions.¹⁰⁷ The first version of UCP was introduced by the International Chamber of Commerce (herein after ICC) in its 1929 congress held in Amsterdam.¹⁰⁸ However, it lacks wider acceptance. It was just endorsed only by France and Belgium.¹⁰⁹ After a through revision, the UCP was re-introduced by the Commission on Banking Technique and Practice of the ICC at Vienna Conference in 1933.¹¹⁰ This version of the UCP got acceptance from some European and USA Banks.¹¹¹ However, it failed to get the acceptance of international trade leading financial institutions of Britain and Commonwealth countries.¹¹²

World War II delayed the continuous revision of the UCP. With the immense effort of ICC, the revised version of UCP again realized at Lisbon Conference in 1951. The revision was meant to keep up the changes and improvements of the international trade. It broaden the worldwide acceptance of UCP. Many of the African and Asian banks endorsed the UCP at this stage, however, Britain and Commonwealth countries insist on their position of rejection.¹¹³

The ICC come up with another revision of UCP in 1962 with collaboration of United Nations Commission on International Trade Law (herein after UNCITRAL), as well as banking organizations of socialist countries. It introduced the major breakthrough and worldwide acceptance of UCP. At this stage Britain and Commonwealth Countries accepted the instrument. Latter on, further revisions and improvements of UCP were conducted. It was revised in 1974 and it became applicable by several banks of 162 countries across the world. Another revision was again made in 1983 (effective 1 October 1984). It was named as UCP400 and intended to overcome challenges faced by international trade due to development of technological communications.

¹⁰⁶Hamid, *Documentary Letters of Credit*, pp. 110-111

¹⁰⁷ Id, p. 111

¹⁰⁸ Reinhard, *Documentary Credits in Practice*, p. 48

¹⁰⁹ Hamid, *Documentary Letters of Credit*, p. 111

¹¹⁰ Ibid

¹¹¹ Reinhard, *Documentary Credits in Practice*, p. 48

¹¹² Zsuzsanna, *Documentary Credits in the International Commercial Transactions*, p. 6

¹¹³ Ibid

Further improvement of UCP 400 was made in 1993 at the ICC conference held in Mexico. It became effective in January 1994 with a name UCP 500. It introduced typical elements to the UCP 400 such as the concept of advising bank and the notion of examination and rejection of documents under letter of credit.¹¹⁴

The latest version of UCP was adopted in 2007 as UCP 600. It brought further improvements in the UCP and widely recognized as business friendly international letter of credit rule. Reduction of unnecessary provisions, clarifications of some sensitive terms under the instrument, exclusion of revocable letter of credit from its ambit, clarification on the scope of examination and rejection of documents by bankers are some of the improvements made under the latest version.¹¹⁵

2.6.2. Supplement to the Uniform Customs and Practice for Documentary Credit for Electronic Presentation (eUCP)

Due to technological improvements electronic and computerized commerce became a major phenomenon in international trade. UCP which is designed for paper based transactions became less important for these transactions. In 2000 the ICC Banking Commission realized the need to address electronic submission of documents in the international trade. The banking commission reported the “steady replacement of paper documents by electronic presentations”, hence, there needs to have guidance and rules like the UCP for the electronic equivalents of paper credits.

Accordingly, the ICC Banking Commission adopted a separate legal framework for electronic letter of credit called eUCP in 2001 at Frankfurt and it came to force in the 1st of April 2002.¹¹⁶ Basically, it is introduced to supplement UCP in order to accommodate presentation of electronic records alone or in combination with paper documents.¹¹⁷

2.6.3. International Standard Banking Practice

The International Standard Banking Practice for the Examination of the Documents under Documentary Credits, which usually named as ISBP, is introduced by the ICC in its meeting at Rome in October 2002.¹¹⁸ It is a practical explanation of UCP on examination and rejection of documents under day to day letter of credit operation of bankers.¹¹⁹ It is helpful for banks, insurance

¹¹⁴ Hamid, *Documentary Letters of Credit*, p. 112

¹¹⁵ Ibid

¹¹⁶ Zsuzsanna, *Documentary Credits in the International Commercial Transactions*, p. 9

¹¹⁷ The Supplement to the Uniform Customs and Practice for Documentary Credit for Electronic Presentation 2002, V1.1, Article e1 [Herein after eUCP]

¹¹⁸ Zsuzsanna, *Documentary Credits in the International Commercial Transactions*, p. 10

¹¹⁹ Ibid

companies, logistic specialists, corporates and freight forwards.¹²⁰ It has functions, among other things, explain terms and conditions of the UCP, specification of elements which are not addressed under the UCP, management of errors in the documents and preparation of insurance documents.¹²¹ At this point it must be clear that by any means application of ISBP neither amend the UCP nor exclude the application of the latter.

2.6.4. Uniform Rules for Bank-to-Bank Reimbursements under Documentary Credits

The 1974 revision of UCP denote the increase of letter of credit usage in the international trade and marked the involvement of third bank (corresponding bank) in the process. The corresponding bank after payment and/or fulfillment of its obligation towards the beneficiary will inevitably require reimbursement (of the whole amount of money it paid to the beneficiary plus service charge) from the issuing bank. Until 1996, however, there were no uniform international rules that regulate bank-to-bank reimbursement. Rather, it was operated via locally accepted practices. Secretary General of the ICC explained the situation as follows

“It had become clear that, while the UCP was the international standard for documentary credit operations, the huge growth in the volume of inter-bank currency reimbursements remained largely subject to local accepted practice in the major financial centers...where banks had formulated their own operating rules.”¹²²

In order to formulate international bank-to-bank reimbursement rules, the ICC established a Working Group in 1993. The Group documented different practices, recognize diverse views and choose best practices.¹²³ Finally, the Working Group come up with Uniform Rules for Bank-to-Bank Reimbursements under Documentary Credits (referred as URR) and published by the ICC in 1995 as URR525. The latest revision of URR adopted by the ICC in 2008 which named as URR725. The application of URR is subject to the parties' agreement. Mere agreement of the parties for the application of UCP does not automatically confer for the application of URR.¹²⁴

¹²⁰ Hamid, *Documentary Letters of Credit*, p. 114

¹²¹ Ibid

¹²² Zsuzsanna, *Documentary Credits in the International Commercial Transactions*, p. 11

¹²³ Ibid

¹²⁴ UCP600, Article 13(a)

2.7. Legal scope of the ICC Letter of Credit Rules

As discussed herein above, the International Chamber of Commerce enacted various rules (such as UCP, eUCP, ISBP and URR) applicable on letter of credit transactions. These rules indeed get worldwide acceptance. However, their application and respective legal force is not without controversy. The controversy is around the questions of; would national courts are duty bound to apply these rules? Are they applied by the courts generally or in limited circumstances? Is agreement of the parties a necessary precondition for application of these rules?

Judge Gaefele stated that “[t]he practice which is subject to a body of rules formulated by the International Chamber of Commerce is an old one and has been applied by the courts to be extent that it can be said to be a legal rule.”¹²⁵ The statement emphasized the duty of the court to apply these rules in the subject matter as far as they have legal force in that particular situation. The statement seems neutral on the issue of legal force of the ICC rules. It did not say, these rules have or have not legal force with or without the agreement of the parties. Hence, it is not qualified enough to have its own view on the questions raised.

At this juncture a look at the instruments themselves are important. The latest version of UCP (UCP600) take a conclusive view on the matter. Article 1 of the said instrument begins by stating

The Uniform Customs and Practice for Documentary Credits, 2007 Revision, ICC Publication no. 600 ("UCP") are rules that apply to any documentary credit ("credit") (including, to the extent to which they may be applicable, any standby letter of credit) *when the text of the credit expressly indicates that it is subject to these rules*. They are binding on all parties thereto unless expressly modified or excluded by the credit. (Emphasis added)

UCP600 take a conclusive stand that, the rule does not have any statutory status, hence, its application is totally depends on the parties' agreement. Accordingly, the UCP will be applicable if and only if the parties clearly incorporated UCP under their contract (credit). Contracting parties have a right of freedom of contract. This enable them to choose laws of their choice in their private contractual matters subject to mandatory provisions of the laws of the nation.

Alike UCP, other ICC rules also does not have any statutory status. For instance, article 13 (a) of UCP600 stipulate the following on the status of Uniform Rules for Bank-to-Bank Reimbursement

¹²⁵ B Maripe, 'The legal aspects of documentary credits in international trade: the case for Botswana', *The Comparative and International Law Journal of Southern Africa*, 1997, Vol. 30, No. 2, pp. 199-207, at p. 200 [Herein after B Maripe, *The legal aspects of documentary credits in international trade*]

If a credit states that reimbursement is to be obtained by a nominated bank ("claiming bank") claiming on another party ("reimbursing bank"), *the credit must state if the reimbursement is subject to the ICC rules for bank-to-bank reimbursements in effect on the date of issuance of the credit.* (Emphasis Added)

It is clear that ICC Bank-to-Bank Reimbursement Rule will not be applicable without a clear agreement of the parties under the credit. The same is true on eUCP and ISBP.

It is needless to say that there are few countries, notably Germany, that confer statutory status to the ICC Rules due to their uniform usage for long period of time.¹²⁶ They conferred with a status of customary law.¹²⁷ Therefore, "the rules can be applied, even if not expressly agreed upon, if they are used regularly in similar transactions and their application could justifiably be expected"¹²⁸

To the writer's opinion, however, it is more reasonable to take the intention of the ICC and wording of the instruments themselves. As a matter of fact they are rules designed to be soft law and will be applicable with a very condition of parties agreement. Zsuzsanna Tóth clearly explain such feature of the ICC Rules, he precisely addressed that "...UCP is neither an international convention, nor it is a law. It is not an international convention as it does not create a formal agreement between states nor it is law, as the ICC, being a non-governmental organization, does not possess legislative authority."¹²⁹

The ICC rules, in particular UCP, are usually rejected by both common law and civil law countries when it come into conflict with the forums regulatory rules and public policies.¹³⁰ Due to the fact that the UCP has no independent legal effect, the national laws of a country or perhaps international laws will carry more weight in a lawsuit concerning a dispute about the interpretation of the stipulations in a credit.¹³¹

2.8. National Law

As of early it was only few countries that have specific statutory rules applicable on letter of credit transactions. The most eyes breaker national law was introduced in the United Kingdom as of the half of 19th Century. It is recognized as the earliest letter of credit rules. United Kingdom is the

¹²⁶ B Maripe, *The legal aspects of documentary credits in international trade*, p. 201

¹²⁷ Ibid

¹²⁸ Id, 200

¹²⁹ Zsuzsanna, *Documentary Credits in the International Commercial Transactions*, p. 8

¹³⁰ Boris, *Legal Aspect of Letter of Credit*, p. 269

¹³¹ Reinhard, *Documentary Credit in Practice*, p. 52

country that refused to recognize ICC Rules for long period of time until 1962. It was basically caused by the desire of the state to retain exclusive regulation of letter of credit via its local legal frameworks.¹³² United Kingdom's letter of credit laws are basically developed through court cases.¹³³

The other prominent country that introduce letter of credit statutory law is United States of America. Through a joint effort of American Law Institute and the conference of commissions on Uniform State Laws¹³⁴, USA codified UCC in 1952 to regulate commercial transactions, including letter of credit.¹³⁵ Article 5 of the UCC, specifically, designed to regulate local, interstate and international letter of credit transactions. It is a well-crafted legislative enactment of contemporary letter of credit practices that combine both technical and legal concepts of letter of credit.¹³⁶ Article 5 of the UCC was revised in 1995 and a more comprehensive and advanced regulatory framework is introduced. The revised provision make article 5 of the UCC more flexible on the source of law of letter of credit by stating that “the effect of this article may be varied by agreement or by a provision stated or incorporated by reference in an undertaking.”¹³⁷ It conformed continuous improvement of letter of credit practices through “custom, usage and agreement of the parties”¹³⁸ It is comprehensive enough to accommodate new forms and features of letter of credit, such as electronic letter of credit, arise in the current commercial context.¹³⁹ It also tried to codify court decisions and prominent scholarly recommendations.¹⁴⁰

USA and UK are not the only states which have their own rules applicable on letter of credit transactions. The limitations on the international letter of credit rules and the desire of states to impulse public policies urge some jurisdictions to promulgate their own letter of credit statutory rules. In a survey concluded for the International Encyclopedia of Comparative Law in 1972 some other countries such as Colombia, Czechoslovakia, Germany, Italy, Lebanon, El Salvador, Greece,

¹³² Zsuzsanna, *Documentary Credits in the International Commercial Transactions*, p. 29

¹³³ Frank, *Letters of Credit with Focus on the UCP 600*, p. 3

¹³⁴ Zsuzsanna, *Documentary Credits in the International Commercial Transactions*, p. 31

¹³⁵ “History of Uniform Commercial Code”, at <https://en.wikipedia.org/wiki/Uniform_Commercial_Code> [last accessed 10 March, 2018]

¹³⁶ Boris, *Legal Aspect of Letter of Credit*, p. 270

¹³⁷ Uniform Commercial Code Revised Article 5, Letter of Credit Section 5—103(c) [Herein after UCC]

¹³⁸ *Id.*, Section 1—102(2)

¹³⁹ Zsuzsanna, *Documentary Credits in the International Commercial Transactions*, pp. 31-32

¹⁴⁰ *Id.*, p. 33

Guatemala, Honduras, Lebanon, Mexico, India, and Syria have their own domestic letter of credit laws.¹⁴¹

Alike the experience of some jurisdictions, Ethiopia has its own national letter of credit laws since 1960 as of the enactment of the Commercial Code. Along with developing a separate legal framework, letter of credit transactions are subject to statutory, quasi-statutory and court decisions scattered in the country's legal frameworks, such as; in the contract law, commercial and/or trade laws, criminal laws, and import and export regulations. Specifically, relevant provisions of the 1960 Civil Code of Ethiopia, Banking Business Proclamation No. 592/2008 and several Directives and Circulars issued by NBE¹⁴² are worth mentioning.

¹⁴¹ See letter of credit laws of different jurisdictions mentioned by Hamed Alavi in his Article (Hamed Alavi, 'Documentary Letters of Credit, Legal Nature and Sources of Law' *Journal of Legal Studies*, 2016, Vol. 16, Issue 31, pp. 106-121, at p. 111). The following are instances of letter of credit laws of different jurisdictions. Czechoslovakian International Trade Code, Act. No. 101 of Dec. 4, 1963; Colombian Commercial Code, arts. 140815 (1971); Guatemalan Commercial Code, Articles 758-765 (1970); Honduran Commercial Code, Articles 898-910; Lebanese Commercial Code, Article 313 (1942); Syrian Commercial Code, Article 418 (1949); German Democratic Republic, Law on International Economic Contracts of Feb. 5, 1970 (GBI, I, 61) Part 8, Chapter 6; Greek Decree Law of July 17, Aug. 13, 1923 (Kd. Them. 582-92), Articles 24-34; Mexican LTOC and so on.

¹⁴² See Directive No. FXD/07/1998; FXD/13/2000, National Bank of Ethiopia, Amendment to Directive No. FXD/07/1998, 18 February 2000; FXD/16/2001, National Bank of Ethiopia, Amendment to Directive No. FXD/07/1998, 29 March 2001; FXD/19/2001, National Bank of Ethiopia, Amendment to Directive No. FXD/07/1998, 01 December 2001; FXD/22/2004, National Bank of Ethiopia, Amendment to Directive No. FXD/07/1998, 19 March 2004; FXD/26/2004, National Bank of Ethiopia, Amendment to Directive No. FXD/07/1998, 01 January 2005; FEC/43/97, National Bank of Ethiopia, Exchange Control Directive Regarding Trade Transactions between Ethiopia and Eritrea Directive No. FEC/43/97, 19 December, 1997; FXD/45/2016, National Bank of Ethiopia, Directive on Transparency in Foreign Currency Allocation and Foreign Exchange Management, Directives No. FXD/45/2016 and FXD46/2017, National Bank of Ethiopia, Directive on Transparency in Foreign Currency Allocation and Foreign Exchange Management Directives No. FXD/46/2017, 20 March 2017.

CHAPTER THREE

THE ADEQUACY OF LETTER OF CREDIT REGULATION IN ETHIOPIA

There are significant letter of credit transactions in Ethiopia. Indeed, billions of dollars are transacted through the said instrument in the country's import and export transactions.¹⁴³ As one writer points out, effective application and improvement of the instrument largely depends on existence of adequate legal framework accompanied by effective application.¹⁴⁴ Accordingly, in-depth analysis of the Ethiopian letter of credit legal framework is made in light of the UCP600, UCC and experience of some other relevant jurisdictions.

3.1. Regulation of Vital Operations of Letter of Credit Transactions in Ethiopia

3.1.1. Issuance of Letter of Credit

Issuance or opening of letter of credit is one of the primary cycle in the letter of credit transaction. Once the parties conclude the underlying contract and convinced that the payment should be effected through letter of credit the next step will be issuance of the credit. While dealing the topic of issuance of letter of credit, the main legal issue will be the formality requirements required to conclude such transaction. Form is a distinct solemnity attached to expression of the parties. It is not, however, an agreement by itself, rather it is a manner where mutual consent of the parties appears or terms and conditions of the contract becomes apparent.

Despite silence of the UCP600 some jurisdictions provide formality requirements for letter of credit transactions. In this regard UCC is mentionable. Under Section 5-104, the code specified the formality requirements as follows.

A letter of credit, confirmation, amendment or cancellation may be issued in any form that is recorded and is authenticated (i) by a signature or (ii) in accordance with the agreement of the parties or the standard practice referred to in Section 5-108(e)

The Code puts the formality requirement at a balanced position that in one hand it avoids stringent formality requirements and on the other hand it did not let the credit arrangement to be concluded with sign or conduct. Thus, the credit can be issued with formality requirements of "record" and

¹⁴³ Interview with W/ro Aster Alemu, Customers Relation Officer of Trade Service at Commercial Bank of Ethiopia, on *the overall letter of credit operation in Ethiopia*, 2 April, 2018

¹⁴⁴ Margreth, *Analysis of the Law and Practice Governing Letter of Credit*, p. 5

“authentication”. No limitation on the types of record. Thus, it can be in a document or other electronic records. The requirement of authentication is only to ascertain the identity of the issuer, confirmer or advisor.¹⁴⁵ Authentication can be made, one, through signature. For instance, “a telegram¹⁴⁶ may be a sufficient signed writing if it identifies its sender... [or even]... the authorized naming of the issuer in the advice of the credit is a sufficient signing.”¹⁴⁷

Unfortunately, there is no provision under the Commercial Code of Ethiopia or other regulatory rules which specify the formality requirements of letter of credit. If one looks at the relevant section of the commercial code¹⁴⁸ nothing is said as to the forms of letter of credit.

In the absence of laws in the relevant sections of the Commercial Code, one may resort to the Civil Code to fill this gap. Article 1676 (1) of the Code clearly states that the title on contracts in general (Articles 1675-2026) shall apply to all types of contracts regardless of their nature and irrespective of the parties involved. According to Article 1678 (c) of the Civil Code, form is one of the validity requirements for conclusion of a contract. The provision reads “[n]o valid contract shall exist ... unless the contract is made in the form prescribed by law, *if any*.” (Emphasis added).

According to article 1719 of the Civil Code, as a principle there is no special formality requirement for conclusion of any types of contract. The agreement of the parties is sufficient to constitute a contract. The same provision under sub article 2, however, provides two exceptional situations where special form will be mandatorily required. The first one is, when the parties under their agreement prescribe a special form. Second, when the law itself commends a special form for conclusion of certain contracts.

When I come back to the case in point, as stated earlier there is no provision in the relevant sections of the Commercial Code or other regulatory laws which command a special form for letter of credit. Hence, it is possible to conclude that it is up to the parties to choose their own appropriate forms of letter of credit. This line of argument, though technically correct, would not be compatible to the special nature of letter of credit.

¹⁴⁵ “Electronic letter of credit”, < <http://Law.justia.com/codes/ohio/2006/orc/jd-130503-55d3.html> > [last accessed at 8 May, 2018]

¹⁴⁶ Telegram includes a message transmitted by radio, teletype, cable, any mechanical methods of transmission and the like

¹⁴⁷ James E. Byrne *et al*, ‘An Examination of U.C.C. Article 5 (Letters of Credit)’ *The Business Lawyer*, 1990, Vol. 45, pp. 1521-1643, at p. 1572 [Herein after James E. Byrne et al, *Examination of U.C.C Article 5*]

¹⁴⁸ The Commercial Code of Ethiopia, Book IV, Title III, Chapter 5 of Section 4.

As we know letter of credit is an instrument used to finance a significant amount of money in the international transaction. Besides, it involves complex contractual relations between different parties and sometimes it trigger national interests. These all peculiar features of letter of credit cannot be satisfied without some special formality requirements. In other words, if we let letter of credit to be transacted in sign or conduct, it will jeopardize different interests, including the public one.¹⁴⁹ Some inference can be draw from the Commercial Code in this regard. For instance, Article 959 of the Commercial Code, though it does not specify the formality requirement of the credit, it named the instrument as “documentary credit” that obviously denotes the credit is issued in the form of documents than oral statement, sign or conduct of the issuing bank. Besides, the same provision also stipulates submission of documents by the beneficiary. This makes the letter of credit to be prepared in special forms than any other forms of oral, sign or conduct. Thus, there needs a clear law that specify the formality requirements of letter of credit transitions by taking into account its peculiar features.

3.1.2. Amendment of Letter of Credit

Amendment of letter of credit is a formal revision or addition proposed or made to a letter of credit. The change includes addition, deletion, correction or alteration of the credit.¹⁵⁰ There are several reasons which trigger amendment of the credit. Sometimes, the credit may be made with erroneous conditions. Even in the absence of errors, there might be a need from the side of the parties to amend the credit due to several reasons such as problems relating to the price, production and transportation of the merchandises.¹⁵¹ That makes amendment of letter of credit a usual phenomenon that, in fact, happens one in every two letter of credits.¹⁵² Amendment of letter of credit is dealt under Article 10 and in a limited extent under article 9 and 11 of UCP600. Article 10(a) of the Rule specified that a credit can be amended by agreement of the issuing bank, the conforming bank, if any, and the beneficiary. At this point one will wonder why the applicant is excluded. In doing so, the assumption of the UCP600 is that, the credit is the responsibility of the issuing bank, therefore, the amendment should be entrusted to it. However, the issuing bank

¹⁴⁹ Letter of credit in many scenarios involve public interests. For instance, approval of Foreign Exchange for import transactions are always through Letter of credit, hence, it will be against the interest of the public to allow Foreign Exchange with oral statements or conducts of the parties. Doing so will open ample opportunity for fraudsters and corrupt officials.

¹⁵⁰ *Black's Law Dictionary*, 8th ed., s. v. “amendment”

¹⁵¹ Reinhard, *Documentary Credits in Practice*, p. 124

¹⁵² *Ibid*

cannot simply amend the credit. It will amend after due consultation and instruction of the applicant. Otherwise, the applicant may not approve the payment made by the bank in the amended credit (if it is not consistent with the original one).¹⁵³ It is riskier to the bank to the extent that it may not get the reimbursement payment from the applicant. However, it does not mean that the bank should consult and wait approval of the applicant for amendment of every silly and immaterial errors made in the credit.

In addition to an express agreement of the parties enshrined under Article 10(a) of the Rule, sub article “c” of the same provision introduces the concept of acceptance by performance.¹⁵⁴ It denotes, if the beneficiary failed to give notification as to his acceptance or rejection of the proposed amendment instead, if he provides a complying presentation to the amended credit his action will be considered as acceptance.

The Rule also introduces some prohibitory provisions. Article 10 (e), for instance, prohibit partial acceptance of the proposed amendments. Hence, ant partial acceptance will be considered as rejection. Again, 10 (f) of the same Rule prohibits any statement of precaution that contains a message “the amendment shall enter into force unless rejected by the beneficiary within certain time”. Such kinds of statement cannot have any effect in this regard.

In Ethiopia, however, there is no regulatory framework for amendment of letter of credit. The only indication as to amendment is pointed out under Article 964 (3) of the Commercial Code. It reads “[s]uch undertakings [conformed irrevocable credit] can neither be modified nor cancelled without the agreement of all persons concerned”. However, such provision is not sufficient enough for many reasons. First, it does not deal about amendment of letter of credit in general. Instead, it is restricted to confirmed letter of credit. Thus, amendment of unconfirmed irrevocable credit and revocable credit at all are not covered. Second, it is a very single statement which is not clear enough for application. For instance, it requires the agreement of all persons concerned. The term “all persons concerned” in the provision is vague and it might expose to unnecessary litigations between the parties. Besides, there are matters relating to amendment of credit which are not yet regulated under the Commercial Code. For example matters such as; should partial acceptance in the credit considered as acceptance or should it be considered as rejection? Should silence of the

¹⁵³ Ibid

¹⁵⁴ Garth, *Legal and Practice perspective on Documentary Credit*, p. 84

beneficiary in respect of the proposed amendment considered as acceptance? Is the applicants consent mandatory? And so on are matters that needs to be addressed in the code.

3.1.3. Revocable - Irrevocable Letter of Credit

In the Ethiopian banking industry there are different varieties of letter of credit used in the import and export transactions among them irrevocable and revocable letter of credits are mentionable Classification of letter of credit as revocable and irrevocable credit is usual in all most all jurisdictions. Similarly, Article 961 of the 1960 Commercial Code of Ethiopia classifies letter of credit as revocable and irrevocable based on the obligation of the issuing bank towards the beneficiary.

Revocable credit as the name itself denote it can be amended, canceled or revoked either by the applicant or the banker at any time until the transaction is completed without the agreement of the beneficiary. Prior to the adoption of UCP600, revocable letter of credit is clearly identified as one variety of letter of credit used in the international commerce. Specifically, Article 8(a) of the UCP500 specifies revocable credit is one verity of letter of credit “that can be cancelled or amended by the applicant without prior notice given to the beneficiary.”

The UCP600 repealed the stipulation of UCP500 and exclude revocable letter of credit from its ambit. Article 3 of the said instrument made clear that “[a] credit is irrevocable even if there is no indication to that effect.” The instrument does not contain any provision relating to revocable letter of credit. However, such exclusion cannot bar the parties’ choice of using the revocable credit as UCP is a soft law that can be modified by the parties’ agreement. Article 1 of the instrument itself specified that, the UCP600 rules “are binding on all parties thereto unless expressly modified or excluded by the credit.” Rosmawani¹⁵⁵ correctly explains what article 1 of UCP600 has to say in relation to revocable letter of credit.

This article [article 1 of UCP 600] provides some room for business people who wish to opt for revocable LC by modifying or excluding parts of the Articles. Frequent fluctuation of prices in the open market, especially of commodities and other limited supplied goods, may trigger the use of a revocable LC. It would be useful for the importer to insist on the issuance of revocable LC in order to avoid a sudden increase of price in the country of the exporter before shipment has taken place.

¹⁵⁵ Rosmawani Che Hashim, *The UCP 600 rules in Letter of Credit (LC): Selected Issues*, Proceeding 8th UUM international Legal Conference 2015 (ISBN: 978-967-0910-03-1) 25-26 August 2015, Bandung, Indonesia, p. 279 [Herein after Rosmawani, *The UCC 600 rules in Letter of Credit*]

Coming to the Commercial Code of Ethiopia, Article 962 postulates, revocable credits are not legally binding undertaking between the banks and the beneficiaries as it can be cancelled or modified at any time. The code specifies further that, there is no obligation on the part of the bank to notify the beneficiary as to the cancellation of the credit.¹⁵⁶ However, when such credit is transferred to a branch or another bank the issuing bank will be obliged to notify to the said banks otherwise cancellation or modification thereof would not affect their rights in the credit.

An extended right of the applicant specified in the code (on revocable letter of credit) gives the buyer a higher security and flexibility as the credit can be canceled by the latter at any time by simply requesting his bank to do so.¹⁵⁷ This generally makes the seller (beneficiary) at greater insecurity and uncertainty. It makes the revocable letter of credit unsatisfactory and seldom used in the Ethiopian import and export transactions¹⁵⁸ and international commerce as well.¹⁵⁹ However, it does not mean that it is totally useless. There are still situations where use of revocable letter credit preferable. The first instance is related to the service charge required for revocable letter of credit. As the role and responsibility of banks' in the revocable credit is comparatively lesser the service charge is cheaper. Hence, parties which have good business relationship such as parent and subsidiary companies and intergroup companies have always prefer to use this type of credit.¹⁶⁰ The second scenario is related to mandatory stipulation of NBE. The NBE mandatorily specified foreign exchange approval for import and export payment shall be on the basis of letter of credit.¹⁶¹ Thus, an Ethiopian importer would be obliged to use letter of credit, though not required by the seller. In such a case the importer usually chooses the cheaper and the more flexible kind of credit. That is, indeed revocable letter of credit.

Irrevocable letter of credit, on the other hand, is an arrangement in which the issuing bank, at the request and in accordance with the instruction of the applicant, absolutely undertakes to pay a beneficiary or honor the draft drawn by him upon satisfactions of terms and conditions stipulated in the credit. It is a complete assurance to the exporter that he will be definitely paid by the issuing bank or conforming bank (if the credit is followed by confirmation of correspondent bank(s))

¹⁵⁶ The Commercial Code of Ethiopia, Article 962

¹⁵⁷ Reinhard, *Documentary Credits in Practice*, p. 82

¹⁵⁸ Interview with Ato Ferid Bedru, Customers Relation Officer of International Banking Department at Hibret Bank, on *the import and export letter of credit operation in Ethiopia*, 5 March, 2018.

¹⁵⁹ Reinhard, *Documentary Credits in Practice*, p. 83

¹⁶⁰ Rosmawani, *The UCC 600 rules in Letter of Credit*, p. 279

¹⁶¹ Directive No. FEC/43/97, Article 2.1

provided that the conditions under the credit are satisfied. In this regard, Article 7 of the UCP600 provides that, the issuing bank is irrevocably bound to honor the credit as of the time of its issuance provided that complying presentation is made to the issuing bank itself or to the corresponding bank, if any. Unlike revocable credit, irrevocable letter of credit cannot be cancelled, modified or amended without the clear consent of the beneficiary, issuing bank and the conforming bank, if any.

The Commercial code of Ethiopia adopts the same stipulations regarding irrevocable credit. According to article 963 of the Code, irrevocable letter of credit is a definite undertaking by the issuing bank to duly fulfill the payment, acceptance and negotiation provisions contained in the credit so long as documents are presented in line with terms and conditions of the credit. However, the code is failed to specify the conditions for cancellation or otherwise amendment of the irrevocable credit. Hence, it needs to be addressed clearly.

So far we have been dealing cases where the credit itself clearly specified as to whether it is/it is not subject to cancellation or amendment without the beneficiaries consent and notification. However, in practice this is not always the case. The credit or the documents establishing it may be silent as to whether the credit is revocable or irrevocable. In this regard, countries address the presumption of revocability or irrevocability of letter of credit in their laws. Majority of the countries such as Germany, Bulgaria, Egypt, Greece, Honduras, Slovakia, Tunisia, United Arab Emirates and United States of America specified that the credit is presumed irrevocable unless the parties expressly agreed otherwise. But still there remains few, namely; Bahrain, Bolivia and Russia prefer to give a presumption of revocability.¹⁶²

So long as our commercial code concerned, it takes the presumption of revocability of the credit in case when the credit is silent as to its status. Article 961 specified that “[u]nless otherwise provided, the credit is deemed to be revocable even if it has been opened for a specific period.” Such a choice of presumption of revocability of the credit in the code was not triggered by the commercial reality of Ethiopia. Rather it is because, the provisions under documentary credit section of the Commercial Code is verbatim copy of the oldest version of UCP, 1951 version. The

¹⁶² Zsuzsanna, *Documentary Credits in the International Commercial Transactions*, P. 22

presumption of revocability of letter of credit first formulated in the 1933 version of UCP.¹⁶³The presumption was not modified in the 1951 version of the Rule.

The ICC, however, amended the UCP for five times in 1962, 1974, 1984, 1994 and 2007 after the 1951 version. In these amendments the ICC avoided the presumption of revocability of the credit and re-endorsed the reverse one. For instance, Article 6 of UCP500 call for the parties to plainly indicate the status of their credit (its status of revocability or irrevocability). In the absence of such specification, the credit will be presumed irrevocable. Such stipulation is reaffirmed under the latest version of UCP. It makes clear that “[a] credit is irrevocable even if there is no indication to that effect.”¹⁶⁴ In this regard, Professor Gutteridge advised that whenever the bank desires to reserve the right to cancel or modify the credit, there should be a clear stipulation on the face of the credit itself. Thus, absence of stipulation should be constructed as irrevocable.¹⁶⁵ Otherwise appreciation would be antagonistic to the custom and usage of the banking industry. This position has also support from case laws. In a case *Foglino v. Webster*, the court decided that a presumption of irrevocability should be sanctioned in case when the credit is silent or ambiguous.¹⁶⁶

The commercial reality and banking practice of letter of credit operations in Ethiopia also suggests that whenever the credit or its establishing document is silent, the credit should be endorsed as irrevocable letter of credit.¹⁶⁷ Therefore, the presumption of revocability of letter credit enshrined under article 961 of the Commercial Code should be reconsidered and the presumption of irrevocability should be endorsed.

3.1.4. Confirmation of Letter of Credit

Confirmation is one among the vital operations of letter of credit transactions. The concept of confirmation of letter of credit arises from the concept of classification of the credit into conformed and unconfirmed. Basically, the classification is based on the undertaking of the correspondent bank towards the beneficiary. An illustration will better explain the matter. A Chinese importer requests his local bank to open letter of credit for the benefit of Ethiopian exporter. However, the

¹⁶³ א. גילדור and A. Gildor, ‘Irrevocable Documentary Credit and Uniform Customs and Practice for Documentary Credits’, *Quarterly Banking Review*, 1969, Vol. 34 , pp. 72-80, at p. 78 [Herein after א. גילדור and A. Gildor, *Irrevocable Documentary Credit*]

¹⁶⁴ UCP600, Article 3

¹⁶⁵ א. גילדור and A. Gildor, *Irrevocable Documentary Credit*, p. 77

¹⁶⁶ *Id.*, p. 78

¹⁶⁷ Interview with Ato Alebacew Fasil, Loan and Trade Finance Customers Relation Officer at Oromia International Bank, on *the types of letter of credit used in the Ethiopian Banking practice*, 3 April 2018

Ethiopian exporter may not know the creditworthiness of the Chinese bank and it will be very comfortable for him if the credit is conveyed by the bank in his locality, Ethiopia. Upon request of the issuing bank, if the Ethiopian bank accepted such a role, then, it will be correspondent bank to that specific credit. Afterward, the credit will be confirmed or unconfirmed based on the level of responsibility the Ethiopian bank assumes towards that particular credit.

Confirmed letter of credit is a credit to which a conforming bank has added its confirmation on it.¹⁶⁸ The confirming bank assumes a definite undertaking, in addition to the issuing bank, towards the beneficiary to honor a draft or other demand for payment made by the beneficiary, as long as the draft or demand complies with specified conditions.

Article 2 of the UCP600 defined confirmation as a definite undertaking by the conforming bank to honor or negotiate a complying presentation. It further clarifies the obligation of the conforming bank towards the beneficiary. Article 8 of UCP600 specified that, once the confirmation is endorsed by the correspondent bank, it will be irrevocably bound to honor the credit as of the time of its confirmation provided that complying presentation is made to the conforming bank or to another nominated bank, if any. Similar approach is followed by other jurisdictions. For instance in a case *Hamzeh Malas and Sons v. British Imex Ltd*, the English Court illustrated the very nature of confirmed letter of credit.

[A] confirmed letter of credit constitutes a bargain between the banker and the vendor of the goods, which imposes upon the banker an absolute obligation to pay, irrespective of any dispute there may be between the parties as to whether the goods are up to the contract or not... A vendor of the goods selling against a confirmed letter of credit is selling under the assurance that nothing will prevent him from receiving the price¹⁶⁹

Further variety of confirmed credit, namely “silent confirmation” is developed in some jurisdictions. Despite the application of such variety in the banking industry, the UCP is silent on the matter. According to Article 2 of the UCP600, confirmation is only by the authorization or request of the issuing bank. Hence, there is no legal framework for the so called silent confirmation. Some jurisdictions recognize such variety in their legal framework. Silent confirmation is an undertaking by the conforming bank without the authorization or request of the issuing bank to honor the complying presentation of the beneficiary. For instance in a case *Mees*

¹⁶⁸ Union Bank of India, Types of LC, p. 9

¹⁶⁹ Hamzeh Malas & Sons V. British Imex Ltd., [1958]2 Q.B. 127

Pierson NV v. Bay Pacific (S) Pte Ltd,¹⁷⁰ the Court recognizes confirmations made by the plaintiff though the credit was confirmed by the plaintiff without authorization of the issuing bank.

The Ethiopian Commercial Code under article 964 (1) specifies that, confirmation of credit is a definite undertaking by the conforming bank as of the date of its conformation towards the credit. The code adopts a clear stand that confirmation can be endorse only to an irrevocable credit. In other words, there is no confirmation for revocable credit. Pertaining to this, the writer believes, this is an appropriate stand.

The Commercial Code makes clear that confirmation can only be at the authorization of the issuing bank. But a question arises what will be the effect if an Ethiopian Bank conform the credit without authorization of the issuing bank? Unlike experience of other countries the Commercial Code is silent in this respect. Meaning, the concept of silent confirmation of letter of credit is not addressed in the Ethiopian legal framework.

At this juncture, one may raise a question that, how can we resolve the issue of silent confirmation with the existing contract laws? Pending the need for specific rules in the Commercial Code, the temporary solution can be characterizing such confirmation as a separate contract than confirmation of a credit in the ordinary sense. As a result the issuing bank will not be duty bound to reimburse the conforming bank's debt that arises from the latter's silent confirmation. This solution is in line with the principle of 'privity of contract' incorporated under article 1952 of the Civil Code. Any contract can produce effects only as between the contracting parties. Hence, a contract of confirmation concluded between the conforming bank and the beneficiary should have effect among themselves only. The issuing bank that is not part of the contract should not be affected by the contract.

3.1.5. Advising the Credit

The concept of advising the credit comes to at hand when the credit is unconfirmed. Because when the credit is unconfirmed the corresponding bank did not assume any responsibility of conforming the credit towards the beneficiary. Rather, its responsibility, as an agent to the issuing bank, is limited to advise the credit. The bank with the aforesaid role usually referred as advising bank.

The UCP600 restrict the responsibility of the advising bank to advise the credit.¹⁷¹ What does it mean by advice the credit is elaborated under article 9 of the same rule.

¹⁷⁰ Mees *Pierson NV v. Bay Pacific (S) Pte Ltd* [2000] 4 SLR 393 (Singapore)

¹⁷¹ UCP600, Article 2

By advising the credit or amendment, the advising bank signifies that it has satisfied itself as to the apparent authenticity of the credit or amendment and that the advice accurately reflects the terms and conditions of the credit and conditions of the credit or amendment received.

Thus, according to the UCP600, the responsibility of the advising bank is checking the apparent authenticity of the document and advise the beneficiary accordingly. For instance, if it found the credit or accompanying documents problematic it should inform the beneficiary without delay. In any case the advising bank is not responsible to honor or negotiate complying presentation of the credit.¹⁷²

Other jurisdictions also specified the concept of advising the credit in their respective legal framework. The case *Cape Asbestos Co v. Lloyd's Bank*¹⁷³, is a best example in this regard. The defendant bank, Lloyd's Bank, become a corresponding bank for a credit issued in favor of the plaintiff. The bank advised the credit without assuming any responsibility of conformation. To the dismay of the plaintiff, the credit was cancelled by the importer before the transaction was completed. Due to this, the plaintiff's attempt to receive the payment from the defendant was futile. Hence, it brings a law suit against the advising bank for payment of the value in the credit. The court decided that, the bank's role is limited to advising the credit, not conforming it. Therefore, it is entitled to refuse acceptance of the draft and effect payment upon it.

When we come to the Ethiopian legal framework, unfortunately, the Commercial Code did not have any provision that deals about advising the credit. Nor it has the concept of unconfirmed letter of credit or the so called advising bank. Thus, what is unconfirmed letter of credit, how it can be advised by the advising bank and what are the responsibilities of the advising bank in this regard are questions that need to be addressed in the code. The problem in this regard is exacerbated due to absence of any regulation or directive that can fill the said gap. The case *Grain Trade Enterprise v. Commercial Bank of Ethiopia*¹⁷⁴ is a good example to show the problem. It is a case instituted by the plaintiff against Commercial Bank of Ethiopia (herein after CBE) for payment under the credit while the bank undertakes only to advise the credit without assuming any responsibility of conformation. In the case, the parties and the court fall on the verge of difficulties for absence laws

¹⁷² UCP600, Article 9(a)

¹⁷³ *Cape Asbestos Co v. Lloyd's Bank* [1921] W.N. 274

¹⁷⁴ *Grain Trade Enterprise v. Commercial Bank of Ethiopia*, Federal High Court, 2006, Civil Case No. 134400 [unpublished]

in the Commercial Code or elsewhere of the legal framework that deals about advising the credit (for details of the case, *infra Section 3.4.4 of the study*).

3.1.6. Negotiation of Documents under Letter of Credit

Negotiation of documents under letter of credit comprises presentation of documents by the seller, examination of documents by the bank and lastly, honoring complying presentation.¹⁷⁵ Negotiation of documents customarily held at the issuing bank and if the credit is conformed, at the locality of the conforming bank.¹⁷⁶ Let us separately discuss elements of negotiation of letter of credit.

3.1.6.1. Presentation of Documents

In trade across national boundaries both parties are curious about the risks inherent in the international trade. The seller wants to minimize the risks that he might face due to long distances, foreign laws, different in currencies and political upheavals. Hence, he requires payment of the purchase price upon conveyance of the ordered products. The buyer on the other hand wants to curtail the risk of paying the purchase price for goods which is not the quantity, quality and other specifications indicated in the contract. To mitigate the antagonistic interest of the seller and the buyer the letter of credit is devised. Accordingly, the seller will be paid upon shipment of the goods with a strict condition that he present all necessary documents as specified in the credit.

Presentation of document is the cornerstone of the letter of credit transactions. Unless the credit is a 'clean letter of credit'¹⁷⁷ presentation of documents is an indispensable integral part of letter of credit.¹⁷⁸ The question that might come in the mind of every reader is, what kinds of documents are required under letter of credit transactions. It is an easy question to ask but difficult to find a precise answer to it. Letter of credit is versatile instrument that can be used for any transaction of goods and services in the international and domestic trades as well. Thus, it is impossible to draw a comprehensive demands, as to the type, number, form and content, for all types of documents under letter of credit transactions. Each transactions specified what kinds of documents are required for complying presentation. However, still there are some common documents usually

¹⁷⁵ Nicholas, *Letter of Credit*, p. 236

¹⁷⁶ Ibid

¹⁷⁷ It is one variety of letter of credit that does not require documentation for acceptance or negotiation of a draft under letter of credit transaction.

¹⁷⁸ William, *Commercial Letter of Credit*, p. 544

required under credit transactions. Some countries specified documents which are vital for import and export transactions in their jurisdiction.

Majority of the provisions of UCP600 deals about documents called under letter of credit transactions. The ICC tried to provide regulatory rules of documents under the credit as detail as possible with a view to avoid difficulties related to it.¹⁷⁹ The UCP600 provides the following documents of letter of credit with their detailed requirements.

i. Transport documents

Transport documents serve as link that connects the interest of the seller and buyer by shrinking the long distance existed between them. With these documents the buyer is assured that the seller ships the goods in accordance with the terms and conditions specified in the credit. It also give a relief for the seller that he will get paid the purchase price upon shipment of the goods without waiting the actual handing over of the goods to the buyer. Besides, the document also denotes the contract between the seller and carrier that the latter accepted the goods for shipment.¹⁸⁰ UCP600 sets out different types of transport documents with their detail formal and substantive parts.

- Multimodal or combined transport documents (Article 19)
- Bill of lading (Article 20)
- Non-negotiable sea waybill (Article 21)
- Charter Party bill of lading (Article 22)
- Air transport documents (Article 23)
- Road, rail or inland waterway transport documents (Article 24)
- Courier Receipt, Post Receipt or Certificate of posting (Article 25)
- Transport documents issued by freights forwarders (Article 26)

ii. Commercial invoice

The commercial invoice is one of the most important document by which the seller requires payment of the purchase price of the goods as indicated in the credit. Customarily commercial invoices mainly contains the description of goods or services with their respective prices.

The UCP600 provides detail regulations of commercial invoices.¹⁸¹ Article 18 (b) and (c) of the rule specified that commercial invoice should contain description of the goods, services or

¹⁷⁹ Reinhard, *Documentary Credit in Practice*, p. 135

¹⁸⁰ Zsuzsanna *Documentary Credits in International commercial Transactions*, P. 68

¹⁸¹ UCP600, Article 18

performance and their respective prices. All the descriptions must correspond with that appearing in the credit. The rule provides an exception that, the bank may accept a commercial invoice issued for an amount in excess of what is permitted in the credit. However, a commercial invoice issued for an amount lesser than what is stated in the credit is unacceptable. To avoid variations in exchange, the invoice must be made out in the same currency as the credit.¹⁸² The Rule further specified that, the invoice should appear to have been issued by the beneficiary and the name of the applicant should also be indicated therein. The only exception to this is when the credit is made to be transferable as indicated under article 38 of the rule.¹⁸³

iii. Insurance documents

Insurance document is issued to insure the object under voyage from the risk of loss or damage. The requirement of insurance documents are detailed under article 28 of the UCP600. Insurance document contains insurance policy, insurance certificate or declaration under an open cover. It should be issued and signed by the insurance company or its agent.

iv. Other documents

Depending on the types of transaction entered, letter of credit may require various documents in addition to transport documents, commercial invoices and insurance documents mentioned herein above. The documents include, but not limited to, certificate of origin, country of origin, certificate of quality of the product and certificate of quantity and weight of the goods.¹⁸⁴

UCP600 provides an open window for documents which might be called in the credit. It is up to the parties to fix the documents they need for complying presentation in the credit. The rule prefer to provide a general rules for any documents which might be called in the credit

If a credit requires presentation of a document other than a transport document, insurance document or commercial invoice, without stipulating by whom the document is to be issued or its data content, banks will accept the document as presented if its content appears to fulfil the function of the required document and otherwise complies with sub-article 14 (d).¹⁸⁵

Article 14(d) of the rule in turn provides

Data in a document, when read in context with the credit, the document itself and international standard banking practice, need not be identical to, but must not conflict with, data in that document, any other stipulated document or the credit.

¹⁸² Id, Article 18(a)-iii

¹⁸³ Id, Article 18

¹⁸⁴ Susmitha, *Documentary Credit Law*, p. 84

¹⁸⁵ UCP600, Article 14(f)

Both articles of the rule emphasized the importance of being cautious when issuing a credit. If the documents or relating matters are not specified by the rule or the credit itself, banks will accept such documents as presented, if its contents does not conflict with any other stipulated documents or the credit itself.¹⁸⁶

As to the time for presentation of documents, Article 29 of UCP600 specified that, presentation of documents should effected at the exact date(s) specified in the credit. Any late submission is unacceptable. The rule further stipulated that, the presentation should be effected at the working hour of the bank. “A bank has no obligation to accept a presentation outside of its working hours.”¹⁸⁷ However, Article 29 (a) provides exceptional ground. When the expiry date of the credit or the last date of presentation falls outside the business day of the bank, presentation can be effected in first following banking day. The bank accepting the presentation should inform such a matter to the issuing bank and conforming bank, if any.¹⁸⁸

Aside to UCP600’s stipulation, UCC section 5-102 specified documents which are commonly required under letter of credit transactions. The documents include draft or other demand, document of title, investment security, commercial invoice or other record, statement or representation of fact, law, right or opinion. The code provides two general requirements applicable to all documents. The first one is, the documents should be presented in a written form or other medium permitted in the credit. At any rate, the document cannot be oral. Second, the documents should be capable of being examined for compliance with terms and conditions of the credit. Unlike UCP600, the UCC prefer to refrain from specification of every detail of the documents. It rather gives such power to the court to interpret the standard practice and determine compliance of the documents in dispute.¹⁸⁹

Under the Ethiopian legal framework presentation of documents are an indispensable integral part of letter of credit transaction. Article 959 of the Ethiopian Commercial Code makes emphasis on presentation of documents.

...documentary credit is a credit opened by a bank providing for payment against *presentation of specified documents* to the opining bank or to its agent. (*Emphasis added*)

¹⁸⁶ Reinhard, *Documentary Credit in Practice*, p. 136

¹⁸⁷ UCP600, Article 33

¹⁸⁸ Id, Article 29(b)

¹⁸⁹ UCC, Sections 5-102 (6) cum. 5-108 (e)

Article 963 also emphasized that the obligation of the issuing bank to pay the beneficiary or honor the draft drawn by him is highly depend on presentation of documents which comply with the terms and conditions of the credit.

Both articles emphasized on presentation of documents by the beneficiary. At this point it is wise to raise a question that, does the Commercial Code has a room for clean letter of credit? Would it fall under the Code's Documentary Credits Section? At this instance, an argument for and against can be raised. The first line of argument may be, the defining provision of the code, Article 959, mentions presentation of documents as a decisive element. Thus, clean letter of credit cannot fall within the ambit of documentary credits of the Code. The second and most plausible argument is, when we critically look the defining provision, Article 959, presentation of documents will be mandatory if and only if the credit itself specified to that effect. The phrase "specified documents" under the said provision has a negative connotation that, documents are not required if the credit does not specify to that effect. Restricting the parties' choice of their letter of credit type with the absence of any provision which prohibit to do so will be against the very essence of freedom of contract. At this juncture the difficult thing is absence of rules that regulate such kinds of credits. Thus, there needs to incorporate provisions that address the case in point.

The obligation of presentation of documents under letter of credit in article 959 has another connotation. Letter of credit cannot have non-documentary conditions that would be verified by the bank in charge of it. The only condition that can be attached with is presentation of documents. The Commercial Code did not have further elaboration of presentation of documents. Unlike the experience of other countries, the Code failed to specify what kinds of documents are required under letter of credit transaction. Nor it specify general requirements for documents that might be called in the credit.

The NBE specified a requirement for presentation of some necessary documents for import¹⁹⁰ and export.¹⁹¹ However, the specification of the NBE is for the purpose of foreign exchange functions only. It does not take into account letter of credit per se. That makes the NBE specification incompatible for all types of letter of credit operations. Thus, there needs to have rule that can effectively regulate presentation of documents for all types of letter of credit transactions.

¹⁹⁰ See Directive No. FXD/07/1998, Article 5.1. For import by letter of credit, the importer needs to submit application form, proforma invoice, trade license, insurance certificate and clearance certificate

¹⁹¹ See Directive No. FXD/07/1998, Article 6.6. for export under letter of credit, the Exporter is required to submit Trade License, Authenticated Letter of Credit, Customs Declaration, commercial Invoice and Sale Contract

3.1.6.2. Honor of Complying Presentation under Letter of Credit Transaction

The main purpose behind submission of a bunch of documents required under the letter of credit by the beneficiary is for payment of the purchase price of the goods or services. Payment is one of the most important reason why letter of credit is designed. The payment may be effected by the issuing bank, conforming bank or nominated bank, as the case may be, provided that the beneficiary submitted documents in line with terms and conditions of the credit.

According to Article 2 of UCP600, credit is an undertaking by the issuing bank or conforming bank, as the case may be, to honor the complying presentation. Honor the complying presentation is an acceptance and payment by the authorized bank according to the modes of payment specified in the credit. The Rule provides the three modes of payment (honor) under its defining provision¹⁹²

To pay at sight if the credit is available by sight payment..., [t]o incur a deferred payment undertaking and pay at maturity if the credit is available by deferred payment..., [t]o accept a bill of exchange ("draft") drawn by the beneficiary and pay at maturity if the credit is available by acceptance.

The rule recognized three payment modes, namely; sight payment, deferred payment and acceptance payment.

Sight payment as the name indicates, the beneficiary will be paid upon presentation of required documents.¹⁹³ Payment by a bank which assume payment undertaking (issuing bank or conforming bank, if any) is without recourse. Once the payment is effected to the beneficiary no repayment can be raised against him.¹⁹⁴

Deferred payment of letter of credit is payable after a certain future date after presentation of the required documents.¹⁹⁵ The exporter may agree with the importer as to the payment for a future date after complying presentation. The payment usually arranges for 30, 60 or 90 days and sometimes for six months depending on the types of transactions they engaged with.¹⁹⁶ Upon complying presentation by the beneficiary, the bank in charge of it will provide a written statement that the former will be paid at the future date specified in the credit. Then, it will be binding against the bank. The beneficiary may ask a discount of the payment before the maturity date of the credit from the bank provided that the discount will be borne by him.¹⁹⁷

¹⁹² UCP600, Article 2

¹⁹³ Nicholas, *Letter of Credit*, p. 236

¹⁹⁴ Reinhard, *Documentary Credit in Practice*, p. 84

¹⁹⁵ Nicholas, *Letter of Credit*, p. 236

¹⁹⁶ Ibid

¹⁹⁷ Zsuzsanna *Documentary Credits in International commercial Transactions*, p. 21

Acceptance payment letter of credit unlike deferred payment credit, is payable after a certain future date upon presentation of required documents. What is different in the acceptance credit is that “the beneficiary should draw and present a bill of exchange together with the documents.”¹⁹⁸ Accordingly, the beneficiary will draw a bill of exchange against the authorized bank. The bank is obliged to guarantee the payment under the draft at the maturity date.

UCC also provide alike specifications with that of UCP600 regarding honor of complying presentation under letter of credit. Section 5-102 of the Code defines honor as “performance of the issuer’s undertaking in the letter of credit to pay or deliver an item of value”. The Code clarifies honor as paying sight credit, accept a draft for acceptance credit and incur an obligation for payment of deferred credit.¹⁹⁹

Coming to the commercial code of Ethiopia, Article 960 specified that the opening bank (issuing bank) has an undertaking to honor complying presentation. However, there is no indication in the code as to what constitutes an honor means. The same provision has some clue on payment modalities under letter of credit. It states “[t]he bank opening the credit shall honour the conditions as to *payment, acceptance, discount or negotiation.*” (Emphasis added). Accordingly, the payment modalities recognized in the commercial code are payment, acceptance, discount and negotiation. However, the code does not have any further clarification of these payment modalities. For instance, the Code does not mention what payment means. Is that to mean sight payment, deferred payment or something different? How the maturity date of payment letter of credit can be calculated also left untouched. The code has stated nothing as what constitutes acceptance, negotiation and discount. What is going to be accepted by the issuing bank? How do we know the maturity date of acceptance letter of credit? How negotiation and discount can be effected? And so on are basic issues that our commercial code failed to address.

3.2. The Doctrine of Autonomy of Letters of Credit and Fraud Exception in the Ethiopian Legal Framework

Letter of credit is the most secured modes of payment in the international commerce. This security emanates from the legal protection it is accorded.²⁰⁰ A number of fundamental legal principles of letter of credit are developed in order to ensure its efficient operation and reinforce it underlying

¹⁹⁸ Reinhard, *Documentary Credit in Practice*, p. 87

¹⁹⁹ UCC, Section 5-102 (a)(8)

²⁰⁰ Garth, *Legal and Practice perspective on Documentary Credit*, p. 45

importance.²⁰¹ One of the most important governing principles is the principle of autonomy of letter of credit. The aim to this subsection is examination of the principle of autonomy of letter of credit and fraud exception in relation to the Commercial Code of Ethiopia.

3.2.1. The Doctrine of Autonomy of Letter of Credit

The word autonomy has a lexical meaning²⁰² of self-governing, independence, self-rule and so on. Etimologically it originates from a Greek word called “autonomia” which means ‘independent.’²⁰³ The word in the context of letter of credit has a meaning of; the credit is independent from the underlying contract, the payment under the credit is solely depend on presentation of complying documents, the role of the bank towards the credit is restricted only to check compliance of the documents to the terms and conditions of the credit and the like.²⁰⁴

In earlier times, there were no conflict on the independence of letter of credit as it was customarily accepted by traders and bankers that the main determinant factor for compliance of the contract is the goods or services specified under the contract. Hence, banks were used to check conformity of the goods as stated in the underlying contract. However, the trend cannot go further due to sophistication and complication of trades across national boundaries.²⁰⁵ Thus, currently recognition of the principle of autonomy of the credit is not a matter of choice.

The purpose of this principle is to create a legal barricade between letter of credit and other contracts accompanying it such as; the underlying contract between the buyer and the seller and a credit agreement between the bank and the applicant.²⁰⁶ The principle makes the obligation of the issuing bank independent from the underlying contract.²⁰⁷

Several literatures provide a bunch of reasons for the necessity of autonomy of letter of credit in todays complicated international transactions. Roberto²⁰⁸ noted that letter of credit “...has a payment function which consists of delimiting the risks in the underlying transaction by allocating

²⁰¹ Jacqueline D. Lipton, ‘Documentary Credit Law and Practice in the Global Information Age’ *Fordham International Law Journal*, 1990, Vol. 22, pp. 1972-1990, at p. 1979 [Herein after Jacqueline, *Documentary Credit Law and Practice*]

²⁰² It is one of defining methods usually used to report the meaning that a word already has in language

²⁰³ Rosmawani *et al*, *Principle of Autonomy in Letter of Credit*, p. 205

²⁰⁴ Ibid

²⁰⁵ Id, p. 206

²⁰⁶ Garth, *Legal and Practice perspective on Documentary Credit*, p. 45

²⁰⁷ Ross P. Buckley & Xiang Gao, ‘The Development of the Fraud Rule in Letter of Credit Law: The Journey So Far and the Road Ahead’, *Penn law journals, U. Pa. J. Int’l L*, 2002, Vol. 23, Issue 4, pp. 663-712, at p.663[Herein after Ross and Xiang, *The Development of the Fraud Rule in Letter of Credit Law*]

²⁰⁸ Roberto Luis Frias Garcia, ‘The Autonomy Principle of Letters of Credit’, *Mexican Law Review*, 2009, Vol. III, No. 1, pp. 67-96, at p. 76 [Herein after Roberto L Frias, *The Autonomy Principle of Letters of Credit*]

each party's liabilities." Accordingly, the seller will be paid by the issuing bank provided that the former present complying presentations. The issuer in turn will be reimbursed by the applicant or it may exercise its right of recourse against the applicant. The applicant does not have a right of recourse against the issuer for breach of the underlying contract. The bank as a paying agent should not be held responsible for inspection of the actual goods or services delivered to the buyer as realistically it would not be feasible²⁰⁹ and will cause unnecessary delay. Overall, several writers refer the principle of autonomy as the cornerstone²¹⁰, foundation²¹¹, crucial, central²¹² and backbone²¹³ of letter of credit. Owing to its importance the principle is reflected and upheld both in the international and domestic legal frameworks.²¹⁴

The principle of autonomy of letter of credit is enshrined under Article 4 and 5 of UCP600. Article 4(a) of the rule reads;

A credit by its nature is a separate transaction from the sale or other contract on which it may be based. Banks are in no way concerned with or bound by such contract, even if any reference whatsoever to it is included in the credit. Consequently, the undertaking of a bank to honor, to negotiate or to fulfil any other obligation under the credit is not subject to claims or defenses by the applicant resulting from its relationships with the issuing bank or the beneficiary.

Article 5 of the rule further emphasizes the effect of the principle on the role of the banks by stating, "[b]anks deal with documents and not with goods, services or performance to which the documents may relate."

The second limb of Article 4(a) of the rule strengthens the principle that the "beneficiary can in no case avail itself of the contractual relationships existing between banks or between the applicant and the issuing bank."

The Rule further sanctions the principle under Article 4(b) as;

²⁰⁹ Employees of the banks are not expert on inspection of goods. They do not have the required qualification for inspecting the quality, quantity, content, substance, taste, smell or physical appearance of all types' goods and services. It is hardly possible and uneconomical for bankers to employ hundreds of thousands of employees who have specialization in each and every goods and service. Due to this, banks only employ workers who are competent on checking documents' conformity towards the specification of the credit and the relevant regulatory rules.

²¹⁰ Roberto L Frias, 'The Autonomy Principle of Letters of Credit', p. 75

²¹¹ Gao Xiang & Ross P. Buckley, 'The Unique Jurisprudence of LCs: Its Origin and Sources,' *San Diego Int'l Law J.*, 2003, Vol. 4, No. 9, pp.119-124, at p.119

²¹² Dolan J.F, *The Law of Letters of Credit: Commercial and Standby Credits*, 4th Edition, Warren, Gorham & Lamont, USA, 1996, p. 480.

²¹³ Davidson, A., *Fraud Exception, the Prime Exception to the Autonomy Principle in Letters of Credit*, Cavendish Publishing Ltd, Australia, 2003, p. 24

²¹⁴ Roberto L Frias, *The Autonomy Principle of Letters of Credit*, p. 75

An issuing bank should discourage any attempt by the applicant to include, as an integral part of the credit, copies of the underlying contract, proforma invoice and the like

The rule take a serious stand on the autonomy of credit. As can be seen from the above quotes it provides detail regulatory rules for the subject matter at hand. The main idea behind these provisions are making a wall between letter of credit and other contacts between the buyer and the seller or credit agreement between the applicant and the issuer. It gives a special emphasis on putting a visible demarcation between the underlying contract and letter of credit. It is to make sure that the former should not intercept in the operation of the latter. As a result, banks will deal with documents as per the terms and conditions of the credit. It does not have any responsibility of inspecting the goods or services to which the documents may relay. Nor the beneficiary can avail himself based on the underlying contract or the credit agreement he has with the issuing bank. Finally, in order to avoid confusion and misunderstanding the banks should discourage any attempt to include any undertakings between the applicant and beneficiary or the applicant and the issuing bank as the integral part of the credit.

The principle of autonomy of letter of credit is also rooted in many common law cases.²¹⁵In this regard I found cases decided by England Courts at the front run. In the case *United City Merchant (Investment) Ltd v Royal Bank of Canada*, Lord Diplock emphasized the principle of autonomy and I quote;

If, on their face, the documents presented to the confirming bank by the seller conform with the requirements of the credit as notified to him by the confirming bank, the bank is under a contractual obligation to the seller to honour the credit, notwithstanding that the bank has knowledge that the seller at the time of presentation of the conforming documents is alleged by the buyer to have, and in fact has already, committed a breach of his contract with the buyer for the sale of the goods to which the documents appear on their face to relate, that would have entitled the buyer to treat the contract of sale as rescinded and to reject the goods and refuse to pay the seller the purchase price.²¹⁶

In the same case Lord Diplock further explains how the principle of autonomy reinforce the very purpose of letter of credit as;

The whole commercial purpose for which the system of confirmed irrevocable documentary credits has been developed in international trade is to give to the seller an assured right to be paid before he parts with control of the goods that does not permit of any dispute with the buyer as to the performance of the contract of sale being used as a ground for nonpayment or reduction or deferment of payment.²¹⁷

²¹⁵ Chumah Amaefule, *The Exceptions to the Principle of Autonomy of Documentary Credits*, p. 27

²¹⁶ *United City Merchants (Investments) Ltd v Royal Bank of Canada* [1983] 1AC 168,183

²¹⁷ *United City Merchants (Investments) Ltd v Royal Bank of Canada* [1983] 1AC 168,183

The case *Sztejn v. Henry Schroeder Banking Corporation* also a landmark court decision where the court upholds letter of credit as independent from the underlying contract between the buyer and the seller. It also adds that, letter of credit is an undertaking by the issuing bank towards the beneficiary for honoring complying presentation.

India also known in its persistent recognition and sanction of the principle of autonomy of letter of credit in its judicial decisions. In this regard, the *Tarapore*²¹⁸ case is mentionable. The court emphasized the principle of autonomy of letter of credit and the respective importance of doing so in terms of encouraging international trade is explained, with its wording;

An irrevocable letter of credit is mechanism of great importance in international trade and so the autonomy of an irrevocable letter of credit is entitled to protection. Any interference with that mechanism is bound to have serious repercussions on the international trade of the country and the courts ought not to interfere with that mechanism except under very exceptional circumstances.²¹⁹

In another case the Indian Supreme Court explained what does the principle denotes in terms of the relationship between the underlying contract and the credit.

“...letter of credit constitutes sole contract with the banker and its authorizing the bank issuing letter of credit has not concern with any question that may arise between the seller and the purchaser of the goods in respect of the purchase price; that there should, however, be strict compliance both by the customer at whose instance letter of credit was issued and by the banker...”²²⁰

The USA also endorse the principle of autonomy of letter of credit in its plentiful court decisions and under the UCC. Specifically the principle is endorsed in the well-known *Sztejn* case.²²¹ The decision emphasizes the barricade between the underlying contract and the credit. In the Court’s wording “letter of credit is independent of the primary contract between the buyer and the seller.” The court added it is not proper and advisable to go behind the documents. To do so, will hamper the instrument’s utility in the international commerce.

The UCC also articulate the principle of autonomy under Section 5-103 (d). The obligations of the issuing, conforming or advising bank under the credit are independent from validity, performance or non-performance of the contracts accompanying the credit. The principle is reinforced under Section 5-108 (1) that fortifies the assumption that the obligation of the issuing bank does not extend to performance of otherwise non-performance of the underlying contract.

²¹⁸ *Tarapore &Co. v. V/O. Tractors Export, Moscow*, (1969)1 S.C.C. 234

²¹⁹ *Tarapore &Co. v. V/O. Tractors Export, Moscow*, (1969)1 S.C.C. 234

²²⁰ *State of Maharashtra v. National Construction Co.* (1996)1 S.C.C.735

²²¹ *Sztejn v Henry Schroder Banking Corporation* (1941) 31 NYS 2nd 631, per Shientag J, at 634

The principle of autonomy of letter of credit is also enshrined in the Ethiopian legal framework. The Ethiopian Commercial Code under Article 959 (2) stipulates “[a] documentary credit is independent of any contract of sale on which it may be based.” The code isolates the credit from any other accompanying contracts and grant the seller an absolute payment right as far as his documents are conforming to the terms and conditions of the credit. Besides, it has the implication that neither the seller nor the bank(s) can challenge payment under the letter of credit by raising breach of the underlying contract. The aforementioned provision underlined that letter of credit is independent of what has been agreed between the seller and the buyer under their sale contract. This principle is reinforced by statements incorporated under article 966 of the Commercial Code;

The bank shall not incur any liability where the documents are on their face in conformity with the instructions received. It shall not incur any obligation in relation to the goods which are the subject of the credit opened.

What is required from the banks are to check whether the documents presented by the seller are comply with the facts stated under the credit. Banks are not required to check the actual shipment of the goods. Any reference whatsoever included in the credit cannot compromise the principle of autonomy.

In an Ethiopian case *Grain Trade Enterprise v. Commercial Bank of Ethiopia*, the Ethiopian Federal High Court address the concept of autonomy of letter of credit

[T]hough the plaintiff argued that it performed its obligation to the importer, reside in Pakistan, in compliance with the contractual terms stipulated in the underlying contract, a look at article 959(2) of the Commercial Code and Article 4(a) of the UCP, letter of credit and the underlying contract are independent of one another. Hence, the plaintiff’s mere performance of the underlying contract does not guarantee him to claim the performance of the credit from the defendant.²²²

In the aforementioned case the defendant, Commercial Bank of Ethiopia undertake the responsibility of advising the letter of credit at hand that is issued by the Abn Amro Bank (Pakistan). One of the argument by the plaintiff (exporter of the good) related to the subject matter is, it performed the contractual obligation in accordance with the contract conclude between the itself and the importer, hence, deserves the payment in the letter of credit that is issued for its benefit despite rejection of the documents submitted by the issuing bank. By raising the principle of autonomy of letter of credit the Court rejected this argument of the plaintiff.

²²² Grain Trade Enterprise v. Commercial Bank of Ethiopia, Federal High Court, 2006, Civil Case No. 134400, p. 12 [Unpublished] (Translated by the author)

The doctrine of autonomy in general operates with an established premise of ‘pay now, sue latter’. Meaning, the buyer should peruse his claims, if any, under the underlying contract by a separate suit against the seller and not by withholding all or part of the credit.²²³ Its force of authority in letter of credit operation is not, however, without any limitation. In this regard, fraud exception is mentionable. Thus, the subsequent topic will address the issue of fraud exception

3.2.2. Fraud Exception

The doctrine of autonomy of letter of credit requires the beneficiary and the bank to honor their respective obligations with trust, commitment and professional integrity. However, this kinds of good business conducts are eroded and the old assumption of ‘the hand shake settles the deal’ proves incompatible in today’s business reality.²²⁴ That is mainly caused by frequent fraudulent acts in letter of credit transactions. It happens, for instance, when there is fraud from the side of the beneficiary. An illustration will better explain the issue. Assume an Ethiopian importer enter into a contract with an Exporter resides in France. They agreed that the exporter will deliver a higher standard of sugar and the importer in return will open an irrevocable letter of credit for the payment. Accordingly, Hibret Bank issued letter of credit at the request of the importer. The fraudster exporter, however, provide false documents to the bank showing that the required sugar were shipped, in fact, it was not the sugar but a dust. This is the situation where the principle of autonomy of letter of credit should be pierced and fraud exception rules should be applied.

The issue of fraud raised in the letter of credit transactions today is timeless and universal phenomenon.²²⁵ It is committed against importers, banks, exporters and the carries of cargo.²²⁶ Technological advancements that intended to enhance commercial transactions at the same time create an opportunity for fraudsters to easily manipulate the transactions. One writer explains, “L/C [letter of credit] fraud is not only widespread, it is big business too, and its tentacles have spread throughout the world.”²²⁷ It has been reported that insurance companies cost millions of

²²³ Chumah Amaefule, *The Exceptions to the Principle of Autonomy of Documentary Credits*, p. 32

²²⁴ Tareq Al-Tawil, ‘Letter of credit and Sale contract: Autonomy and Fraud’, *International Trade and Business Law Review*, 2013, pp. 160-223, at p. 183 [Herein after Tareq Al-Tawil, *Letter of Credit and Sale Contract*]

²²⁵ Chumah Amaefule, *The Exceptions to the Principle of Autonomy of Documentary Credits*, p. 36

²²⁶ Tareq Al-Tawil, *Letter of Credit and Sale Contract*, p. 183

²²⁷ Yanan Zhang, *Approaches to Resolving the International Documentary Letters of Credit Fraud Issue*, Tampereen Yliopistopaino Oy Tampere, Finland, 2011, p. 21 [Herein after Yanan Zhang, *Approaches to Resolving the International Documentary Letters of Credit Fraud Issue*]

dollars each year due to maritime frauds.²²⁸ Due to its enormous undesirable effects, the learned judge Cresswell J describes it as “a cancer in the international trade.”²²⁹

The UNCTAD report shows that, there are basically four kinds of frauds that are usually committed under letter of credit transactions. First, falsification of cargo documents while no goods are in fact shipped. Second, where the goods are inferior in terms of its quality or quantity. Third, where the same goods are sold to two or more persons. Fourth, where cargo documents are issued twice for the same merchandises.²³⁰

The human efforts to combat fraud, specifically fraud in letter of credit, is enormous. In this regard, we need to consult the extent of protections accorded to the letter of credit in terms of preventing fraud in the transaction both in the international and national legal frameworks.

When we think about the international legal framework for regulation of letter of credit, the primary legal instruments are UCP 600 and its supplementary rules. The UCP600 does not contain any provision that deals about the issue of fraud exception; nor does its supplementary rules. There is no fraud exception framework under the relevant provisions of UCP 600, Article 4²³¹, 5²³², 7²³³, 8²³⁴, 14, 15 and 16.²³⁵ The disclaimer incorporated under the Rule emphasizes its position on exclusion of fraud exception from its ambit. The provision itself is self-explanatory

²²⁸ Tareq Al-Tawil, *Letter of Credit and Sale Contract*, p. 183

²²⁹ *Standard Chartered Bank v Pakistan National Shipping Corporation and Others* [1998] 1 Lloyd's Rep 684.

²³⁰ UNCTAD report (2003), UNCTAD secretariat, ‘A Primer on New Techniques Used by the Sophisticated Financial Fraudsters with Special Reference to Commodity Market Instruments’ (UNCTAD/DITC/COM/39), 7 March, 2003, p. 7, at <http://www.unctad.org/en/docs/ditcom39_en.pdf> [Last accessed 12 May 2018].

²³¹ The provision deals about the relationship between the underlying contracts and the credit. it specifically states “A credit by its nature is a separate transaction from the sale or other contract on which it may be based. Banks are in no way concerned with or bound by such contract, even if any reference whatsoever to it is included in the credit. Consequently, the undertaking of a bank to honour, to negotiate or to fulfil any other obligation under the credit is not subject to claims or defenses by the applicant resulting from its relationships with the issuing bank or the beneficiary.”

²³² The provision address the responsibility of the bank in relation to documents in the cred and goods, services and performances in the underlying contract. Specifically it denotes “Banks deal with documents and not with goods, services or performance to which the documents may relate”

²³³ It deals about the obligation of the issuing bank in relation to the letter of credit. The provision denotes that the bank is under obligation to pay the beneficiary as far as the latter’s submission constitutes complying presentation. However, the provision stipulates noting what the bank can do if it learned fraud is committed.

²³⁴ The provision addresses the undertaking of the conforming bank under letter of credit operations. Specifically, the bank is under duty to honor complying presentation made by the beneficiary. However, no stipulation as to fraud exception in this regard.

²³⁵ Article 14, 15, and 16 of UCP600 deals about standard of examination of documents, complying presentation and the issue of discrepant documents under letter of credit operations. According to these provisions, the document will be examined and considered as complying or otherwise discrepant on the basis of the documents alone. Still on these provisions there is no fraud exception on which a different examination standard can be followed or apparent compliance of the documents to the terms and conditions of the credit can be disregarded.

A bank assumes no liability or responsibility for the form, sufficiency, accuracy, genuineness, falsification or legal effect of any document, or for the general or particular conditions stipulated in a document or superimposed thereon; nor does it assume any liability or responsibility for the description, quantity, weight, quality, condition, packing, delivery, value or existence of the goods, services or other performance represented by any document, or for the good faith or acts or omissions, solvency, performance or standing of the consignor, the carrier, the forwarder, the consignee or the insurer of the goods or any other person.²³⁶

Despite the aforementioned provisions, it does not mean that the ICC denies fraud exception. It indeed recognizes fraud exception in its different documents such as documents 470/371 and 470/373 and leave the matter to the national laws and courts. The assumption held by the ICC is that, it is not the role of the UCP to regulate fraud issues as its scope significantly varied among jurisdictions. Thus, it is the national laws and courts that should regulate the matter.²³⁷ Yanan Zhang explains the rationale behind exclusion of fraud rule from the ambit of UCP. He argued that the ICC rules are not rules of law in the strict sense rather they are rules of best banking practice. The issue of fraud, on the other hand, is a matter of rule of law, thus, it should be tackled by the national laws and the courts of the forum.²³⁸

Due to this majority of national jurisdictions acknowledge fraud exception and craft rules to that effect. The rule allows “the issuing bank or a court to examine the facts behind a complying presentation and to disrupt payment if fraud is committed in the transaction.”²³⁹ In this regard, the experiences of United Kingdom and USA are enormous.

For instance in US case, *Old Colony Trust Co. V. Lawyers' Title & Trust Co.*²⁴⁰, the court decided that the seller can object payment in the letter of credit if the documents are illegal or false, though they are correct in their face.²⁴¹

In another well-known case, *the Sztejn Case*²⁴², the court bar the payment in the credit after it learned that some of the documents presented in the credit contain the element of forgery. The court further develops principles for application of fraud exception rules.

²³⁶ UCP600, Article 37

²³⁷ ICC, Opinions of the ICC Banking Commission 1995-1996, ICC Publication No. 565, p. 22

²³⁸ Yanan Zhang, *Approaches to Resolving the International Documentary Letters of Credit Fraud Issue*, p. 68

²³⁹ Frank Roland, *Letters Of Credit with Focus on the UCP600*, p. 35

²⁴⁰ *Old Colony Trust Co v. Lawyer's Title & Trust* [1924] 297 F 152

²⁴¹ Ross and Xiang, *The Development of the Fraud Rule in Letter of Credit Law*, p. 673

²⁴² *Sztejn v. Henry Schroeder Banking Corporation* [1941] 31 NYS 2d 631

- ✓ The independence of banks obligation under the letter of credit should not be extended to protect the unscrupulous seller
- ✓ No interruption of payment under the credit except for the exceptional grounds of fraud
- ✓ Mere allegation of fraud should not be a ground for interruption of payment

The case become influential and steppingstone for many jurisdictions such as; UK and Australia to develop their own fraud exception rules.

Having so many judicial experiences, USA codified its UCC to govern fraud exception in transaction which involves letter of credit. It makes America the first state which established statutory basis for fraud exceptions. The enactment of UCC relief victims of letter of credit from raising contract laws and other principles to demand injection of payment under the credit. Section 5-109(2) (b) of the code specified grounds where the principles of autonomy of letter of credit can be pierced and the fraud exception be applied. The first condition is that, there needs a claim by the applicant whenever the alleged fraud comes to its mind. Then, the court may temporarily or permanently enjoin the payment by taking into account different factors.

UK also recognized the fraud exception long ago. In a case, *Pillans v. Van Mierop*²⁴³, which was decided before two hundred fifty two years ago that the learned Judge Lord Mansfield clearly recognized the principle of fraud exception in a transaction which involve letter of credit. In another case *Societe Metallurgique D'Aubrives & Villerupt V. British Bank for Foreign Trade*²⁴⁴, the court recognized the fraud exception as follows.

First of all, did the person presenting misdescribe [sic] the goods in such a way as to be guilty of fraud.

If that were so, then the bank in refusing to pay would be justified²⁴⁵

In another well-known case, *City Merchants (Investments) Ltd. v. Royal Bank of Canada*²⁴⁶, the court apply the fraud exception and enjoin the payment to a seller who fraudulently pre-dated a bill of lading.²⁴⁷ Even though the fraud rule is recognized long ago, traditionally UK courts are reluctant to pierce the independence of letter of credit and followed very shallow and stringent approach towards the fraud exception.²⁴⁸ They usually require high standard of proof to establish existence of fraud.

²⁴³ *Pillans v. Van Mierop* [1756] 97 Eng Rep 1035

²⁴⁴ *Societe Metallurgique v. British Bank for Foreign Trade* [1922] 11 Lloyd's Rep. 168

²⁴⁵ Ross and Xiang, 'The Development of the Fraud Rule in Letter of Credit Law', p. 671-672

²⁴⁶ *United City Merchants (Investments) Ltd v. Royal Bank of Canada* [1983] A.C. 168

²⁴⁷ Ross and Xiang, *The Development of the Fraud Rule in Letter of Credit Law*, p. 688

²⁴⁸ *Id*, p. 689

When we come to Ethiopian laws and experiences, it has bossy commercial code and nil court practice towards the issue of fraud exception. When we see the commercial code it only incorporates nine provisions, from articles 959 to 967, which are more or less deal about principle of independence, principle of strict compliance, the concept of revocable and irrevocable credit and the respective rights and obligations of the issuing and conforming banks. No provision, even word, is incorporated which deal about the issue of fraud exception.

Absence of rules that resolve disputes related to fraud under letters of credit transaction will put Ethiopian judges in the verge of difficulties. The judges who faced such kinds of cases do have two undesirable options. The first one is, totally avoid the concept of fraud exception and stick to the independence features of documentary credit as mentioned under articles 959 and 960 of the Commercial Code. However, this should not be considered as the choice as it will result injustice against the innocent party who remain with nothing though he performed his contractual obligation dully and effectively. The other option, similar to one of the ancient case of US in the *Higgins case*,²⁴⁹ resort to contract law. As per the provisions of the sale contract enshrined under the Civil Code, the seller is required to guarantee the conformity of the goods as stipulated in the contract, in addition, he should also assure the goods are free from defect.²⁵⁰ Pursuant to Article 2288 of the Code, the goods shall not be deemed to conform to the contract where the seller delivered to the buyer a thing different to that provided in the contract, or a thing of a different species.

When the seller prepare forged documents for payment while he ship rubbish goods or ship nothing at all, there comes nonperformance of the underlying sale contract. At this juncture, the innocent buyer can resort to the relevant provisions of the Civil Code to obtain a remedy by invoking nonperformance of the seller. As a result, the buyer can claim forced performance²⁵¹, purchase in replacement²⁵² or cancellation of the contract.²⁵³ Finally, apart from or in addition to other remedies, the buyer have a right to claim compensation for damage caused to him by the other party who failed to perform his obligation.²⁵⁴

In general, this option focus on bring a law suit based on the underlying contract than focus on withholding the payment in the credit. This option, however, is not appropriate and advisable.

²⁴⁹ *Higgins v. Steinharderter* [1919] 175 NYS 279

²⁵⁰ The Civil Code of Ethiopia, Article 2287

²⁵¹ *Id*, Articles 1771(1), 1790, 2329

²⁵² *Id*, Article 2330

²⁵³ *Id*, Articles 1771(1), 1790 and 2336

²⁵⁴ *Id*, Articles 1771(2), 1790(1) and 2360

Because, the concept of fraud exception is required to enjoin payment of the fraudulent seller in the credit before he actually paid by the bank. In other words, if the fraudulent seller is paid by the authorized bank despite the fraudulent acts the issue of fraud exception will be over. It will be very difficult and onerous to the innocent importer or exporter, as the case may be, to bring a suit based on the underlying contract having the parties are reside in different jurisdictions that are very distant and have different legal systems, languages, political land scape and so on. Hence, by no means it can be taken as a substitute for fraud exception rules. It is rather, the typical way of securing contractual rights. When it is seen in lite of the underlying contract accompanied by letter of credit payment, it will have a message of pay now in the letter of credit and sue latter based on the underlying contract.

Apart from the civil remedies, one can think letter of credit fraud remedy under the Ethiopian Criminal Law. Article 375(a) of the FDRE Criminal Code makes clear that anyone who forge documents with the intent to procure benefit for oneself or for another or to injure the rights or interests of another person is punishable with simple imprisonment for not less than three months, or, in more serious cases, with rigorous imprisonment not exceeding ten years.

Besides, Article 391 through 395 of the Criminal Code outlawed any act of falsification of goods. Thus, a seller who send rubbish goods or crushed stone instead of oil will be criminally liable.

If the fraudster found guilty, the bank can stop the payment and denied the beneficiary as it would be a fruit of criminal acts. It basically emanates from the underline principle of justice, “one should not benefit from his/her own fault.”

It has to be noted that, the criminal remedy is independent from the civil one, hence, they should not be taken as a substitute to one another. It basically emanates from the difference between these remedies. For instance, parties to the civil and criminal remedy are different. Besides, the objectives behind these remedies are also distinct. Moreover, the standard of proof required under the criminal and civil cases are different. Therefore, existence of criminal remedy under the FDRE Criminal Code cannot be an excuse for failure of having fraud exception rules in the Commercial Code.

Therefore, the writer suggests that, Ethiopia needs to adopt or enact fraud exception laws for various reasons. The first reason is to close a loophole. As we know letter of credit does not concern about the underlying contract. This obviously will create a loophole for fraudsters to abuse the

system and receive undue benefits. So that, enacting fraud rule will shrink the loopholes under letter of credit and it will at least minimize the enormity.

The second one is, public policy reason towards controlling fraud. The government, as a responsible organ to correct and suppress acts which can distort the economy of the country, shall enact fraud laws. No one should benefit from his/her own wrong. Therefore, those who involved in fraudulent activities should not be incentivized rather they shall be penalized, be it civilly or criminally.

The last, but not the least, reason is maintaining the utility of letters of credit. Fraud is not only a violation of public policy but also poses a serious threat against the utility of letters of credit.²⁵⁵ Utility of letter of credit highly depends on the fact that it will provide a fair and balancing interest for both of the parties.²⁵⁶ Fraud exception rule is needed to suppress fraudsters, thereby, encourage others to use letter of credit that in turn will increase its credibility in the import and export transactions of Ethiopia.

3.3. The Doctrine of Strict Compliance in the Ethiopian Legal Framework

The doctrine of strict compliance has a strong bond with the principle of autonomy of letter of credit. It reinforces the stand that bankers deal with documents not goods, services or performance accompanying the credit. It is an extension of the principles of general law of agency²⁵⁷ whereby banks, as an agent to the parties, are obliged to determine conformity of documents on the basis of their face along with terms and conditions specified under the credit.

The principle, basically, denotes the fact that documents presented by the beneficiary should be strictly conform to the terms and conditions stipulated under the credit and relevant legal rules. Thus, even a minor discrepancy of the documents may be sufficient enough to reject the documents. This doctrine is first developed in English case, *Equitable Trust Co. v. Dawson Partners Ltd*, Sir John Donaldson stipulates;

There is no room for documents which are almost the same, or which will do just as well . . . the bank which knows nothing officially of the details of the transactions financed cannot take upon itself to

²⁵⁵ Ross and Xiang, *The Development of the Fraud Rule in Letter of Credit Law*, p. 666

²⁵⁶ Ibid

²⁵⁷ Lu Lu, *The Exceptions In Documentary Credits In English Law*, PHD Dissertation, The University of Plymouth, Plymouth Law School, Faculty of Business, 2011, p. 34

decide what will do well enough, and what will not. If it 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.²⁵⁸

According to Sir John's explanation the banker is not concerned with the reason why the beneficiary has called for particular documents and that there is no room for documents which are almost the same, hence, the bank shall ensure strict compliance of the documents tendered by the beneficiary.

Overtime different standards of conformity of documents have been developed. The first one is 'the precise and mirror image' test. It is very strict standard that requires hundred percent conformity of documents to the terms and conditions of the credit. Any minor error, though irrelevant, in the documents are sufficient to deny payment to the beneficiary. The second one is, 'substantial compliance' test. It sets out slack standards of compliance of documents. Inconformity of documents will be compromise as far as the errors are not substantial enough. Third, 'bifurcated standard' test provide a double standard tests for the beneficiary to get payed and the paying bank to get reimbursement from the applicant. Fourth, 'strict compliance' test. It was developed by UK and currently it is accepted by almost all commercial communities in the world. According to this standard, documents should conform in terms of their form, content and type.²⁵⁹

The issue of documentary compliance is dealt under the 1960 Commercial Code of Ethiopia. If we look at Article 965 of the Code, it specifies "[t]he bank shall satisfy itself that the documents *conform strictly* to the instructions contained in the credit." (Emphasis added.) The standard incorporated in our Commercial Code is strict compliance. Thus, the beneficiary should tender documents which satisfy all the descriptions in the credit. The bank which examines the documents, consequently, should not accept documents with the assumption that the documents are almost the same or fair enough. Because, a bank does not have an authority and professional qualification, as well, to determine an appropriate specification of goods, transport documents or insurance descriptions than the parties themselves.

Article 966 of the Commercial Code reinforces the conformity principle by stating "[t]he bank shall not incur liability where the documents are *on their face* in conformity with the instructions received." (Emphasis added). This provision adds one additional element which does not mentioned under Article 965 of the same code. That is, the examination of documents should be

²⁵⁸ Equitable Trust Co. of New York v. Dawson Partners Ltd., (1927) 27 L.J.L.Rep.49.

²⁵⁹ Garth, *Legal and Practice perspective on Documentary Credit*, p. 48

‘as they appear on their face’. This expression of the Code puts the standard at a balanced position that the examining bank should not engage in microscopic scrutiny of documents as so fault finding mission. Equally so, the bank should not examine documents through speculation or guessing. The issue of conformity is also dealt in similar fashion under the UCP 600. Specifically, Article 14 the rule underlines;

A nominated bank acting on its nomination, a confirming bank, if any, and the issuing bank must examine a presentation to determine, on the basis of the documents alone, whether or not the documents *appear on their face* to constitute a *complying presentation*. (Emphasis added)

Complying presentation in this provision denotes a presentation in accordance with the terms and conditions of the credit, the applicable provisions of UCP rules and international standard banking practices.²⁶⁰

The Commercial Code, however, has limitations on sufficiently regulating examination and rejection of documents in letter of credit transactions. The limitation begins from the issue of what kinds of documents are required for letter of credit transaction. The code failed to mention documents that are necessary for letter of credit transaction. As I discussed somewhere else above the UCP and some other jurisdictions require basic documents that may be called in the credit. The documents usually referred are transport documents²⁶¹, insurance documents, commercial invoice and some other relevant documents.²⁶² The writer did not argue that, the code should mention all documents that might be called in the credit as specifying necessary documents in the credit is a task primarily left to the parties’ agreement. As a legal framework, however, stipulation of basic documents have irrefutable importance.

Besides, the Commercial Code lacks any specification for documents that might be called in the credit or by the law. Of course specification of the details of the documents are mainly the responsibility of the parties, especially the applicant. In the commercial reality, however, one cannot expect all traders are meticulous enough to specify every detail of the documents. In such a case, there should be gap filling provisions that might provide general and/or specific

²⁶⁰ UCP600, Article 2

²⁶¹ The Transport documents required in the credit varies depending on agreement of the parties. The possible transport documents are; Multimodal or combined transport documents (see Article 19 of UCP600), Bill of lading (see Article 20 of UCP600), Non-negotiable sea waybill (see Article 21 of UCP600), Charter Party bill of lading (see Article 22 of UCP600), Air transport documents (see Article 23 of UCP600), Road, rail or inland waterway transport documents (see Article 24 of UCP600), Courier Receipt, Post Receipt or Certificate of posting (see Article 25 of UCP600) and Transport documents issued by freights forwarders (see Article 26 of UCP600)

²⁶² The documents include, but not limited to, certificate of origin, country of origin, certificate of quality of the product and certificate of quantity and weight of the goods

requirements. The UCP600 is best example in this regard. It stipulate general requirements for all types of documents, more importantly for transport documents, commercial invoice, insurance and other important documents that might be called in the credit.

The first one is, the documents should strictly comply. As explained herein above, it is considered as one of the most important requirement that demands compliance of the document to the terms and conditions of the credit. As Learned Judge Bailhache affirms “a person who ships in reliance on the letter of credit must do so in exact compliance with its terms.”²⁶³

Second, the documents tendered by the beneficiary should be consistent. Article 14 of UCP600 provide this standard repeatedly. For instance, Article 14 (d) of the same rule specified that the date in the document should not conflict with the date in any other documents or the credit. Article 14 (e) and (f) again stated that, documents other than commercial invoice or transport documents should not conflict with description of the credit.

Third, the documents submitted to the bank should be original unless otherwise stipulated in the credit. Article 17 of UCP600 states, save otherwise stipulation under the credit, at least one original of each document should be submitted. The documents would be considered as original when it bears an apparently original signature, mark, stamp and so on.

Apart from these and other general requirements, UCP600 provide specific requirements that are applicable against each documents such as; transport document, insurance document, commercial invoice and other relevant documents.²⁶⁴

Discrepancy of documents are the usual phenomenon in the letter of credit transactions. It is estimated that documents are compiled as per terms and conditions of the credit in significantly lower degrees of 27 percent only.²⁶⁵ There are dozens of instances in Ethiopia on discrepancy of documents, though, the exact figure is unknown.²⁶⁶ The most common discrepancies are inconsistent date, incorrect or missing signatures, misspelling, missing files, incorrect specifications, mistaken wordings, insufficient coverage and the like against transport documents, invoices, drafts and insurance documents.²⁶⁷

²⁶³ Scottish and Australian Bank Ltd v. Bank of South Africa [1922] 13 Lloyd’s Rep 21

²⁶⁴ UCP600, Article 18 through 28

²⁶⁵ Zsuzsanna *Documentary Credits in International commercial Transactions*, p. 103

²⁶⁶ Interview with Zelalem Asmare, Manager of International Banking Department at Hibret Bank, on *the import and export letter of credit operation in Ethiopia*, 3 April 2018.

²⁶⁷ Frank Roland, *Letters of Credit with Focus on the UCP600*, p. 28

The important point at this juncture is identifying which discrepancies constitute failure of strict compliance. In other word it poses a question that, is that all irrelevant or minor errors constitute noncompliance? The Commercial Code apart from providing the standard of strict compliance it does not limit the application of the principle for minor and irrelevant errors. It practically causes an enormity that banks persistently reject for very silly and irrelevant errors.

The UCP600, however, incorporate limitations for application of the principle for minor discrepancies. Even though strict compliance is the standard for honoring presentation, it is not all discrepancies that results failure of compliance. Some minor discrepancies are excusable. For instance, Article 30(b) of the Rule stipulated that, 5% less or 5% more in the quantity of the goods are tolerable, save otherwise stipulation in the credit. Other tolerable discrepancies are also mentioned under article 30 and 31 of the Rule.²⁶⁸

The other point that should be addressed here is that, what should be done if the documents(s) found discrepant. As usual the Commercial Code is silent. If we look the UCP600 in this regard, it stipulates that, the authorized bank has five working days following the day of presentation to determine compliance or discrepancy of the documents.²⁶⁹ If finally the documents are found discrepant, the bank may refuse to honor the documents or it may approach the applicant for waiver.²⁷⁰ If the applicant did not waive the discrepancy, the bank shall notify the beneficiary no later than the close of the fifth banking day following the day of presentation.²⁷¹

3.4. The parties to the Letter of Credit and Their Mutual Undertakings in the Ethiopian Legal Framework

In the Ethiopian Legal Framework letter of credit is an institutional method of transaction that needs the participation four parties, namely; the applicant (buyer/importer), beneficiary (seller/exporter), issuing bank (opening bank) and corresponding bank (beneficiary's bank). The letter of credit will happen when these parties conclude a chain of contractual relations; (1) the applicant and the beneficiary needs to conclude sale contract (underlying contract), (2) the applicant and the issuing bank needs to agree for issuance of the letter of credit, (3) the issuing bank needs to undertake an obligation in the contract for payment of the beneficiary upon complying presentation, (4) the issuing bank needs to enter into an agreement with the

²⁶⁸ UCP600, Article 30 and 31

²⁶⁹ Id, Article 14(b)

²⁷⁰ Id, Article 16 (a) and (b)

²⁷¹ Id, Article 16(d)

corresponding bank that the latter will serve as advising or confirming bank towards the beneficiary. These chain of the contractual relationship between the parties are normally expected to create contractual rights and duties among the parties. Thus, the aim of this section is to address undertakings' of the parties in letter of credit transaction under the Ethiopian Legal Framework. In this discussion we have to take notice that, the obligation to one of the parties is a right to the other named party.

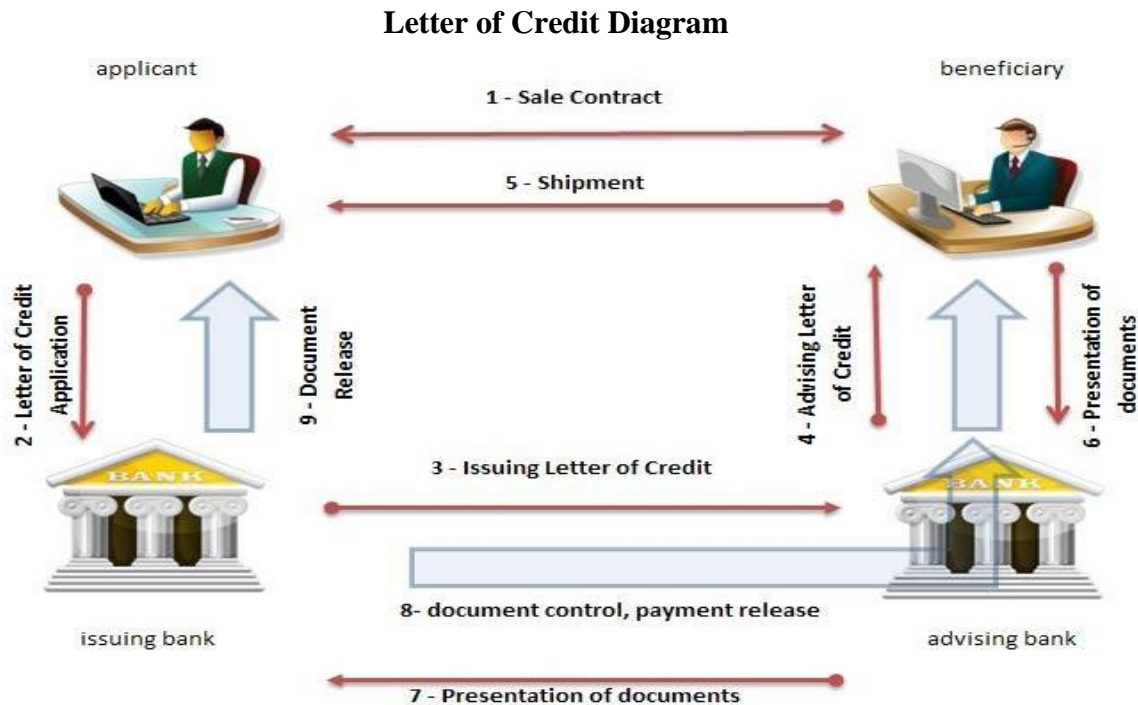


Figure 1: Demonstration of parties to a letter of credit and their mutual undertakings

Source: <http://globalpetroleumpartners.wordpress.com>

Explanation of the diagram

1. It represents the underlying contract conclude between the applicant and the beneficiary.
2. It is an agreement between the applicant and the issuing bank for issuance of the credit
3. It is a contract between the issuing bank and the beneficiary that the former assumes the undertaking of payment provided that the latter provided complying documents
4. It is an undertaking by the advising bank to the beneficiary that the former will advise the credit

5. It denotes the obligation of the beneficiary to deliver the goods ordered to the applicant
6. It shows the obligation of the beneficiary to submit complying documents to the advising bank
7. It denotes the advising bank should forward the documents to the issuing bank
8. Once the issuing bank receive the documents and ascertain their conformity, it will release the payment
9. Finally the documents will be released to the beneficiary upon reimbursing the issuing bank

3.4.1. Undertakings' of the Applicant

There is neither definition nor indication in the Ethiopian Commercial Code regarding the issue of who is the applicant in the letter of credit transaction. The UCP600, however, define it as “a party on whose request the credit is issued.”²⁷² With a certain modification to the UCP600 definition, the UCC defined the applicant as a person at whose request or whose account the credit is opened. It also includes a person who requests the issuer on behalf of another person as applicant as far as he assumes the obligation to reimburse the issuing bank.²⁷³

As a party to the credit transaction, the applicant assumes rights and obligations. Under sale contract in general and international sale of goods in particular, the seller has two main obligations. These are to pay the purchase price and take delivery of the goods.²⁷⁴ However, it is not the intention of the writer to deal the rights and duties of the buyer under sale contract. It rather focuses on the applicant's undertaking in the letter of credit.

The underlying contract as a base for the payment in the credit needs to sufficiently specify details of the letter of credit. One of the primary thing that should be addressed in the contract is the time of opening of the credit. Opening of the credit is one of the prime obligation of the applicant. Depending on agreements of the parties, the applicant is required to open the credit preceding the exporter's duty of shipment of the goods. It is meant to enable the exporter to fulfill his obligations with assurance of the payment. However, it may not be always the case that parties may fail to specify the time of opening of the credit. Thus, there shall be a legal framework which can fill this

²⁷² Id, Article 2

²⁷³ UCC, Section 5-102 (a) (2)

²⁷⁴ See the 1960 Civil Code of Ethiopia, Book V, Chapter 2, Obligations of the buyer. See also United Nations Convention on Contracts for the International Sale of Goods (1980, Vienna), Chapter III, Obligations of the buyer

gap. Unfortunately, nothing has been said in the Documentary Credit Section of the Ethiopian Commercial Code.

Some jurisdictions, however, provide regulatory rules on the issue at hand. In the English case, *Pavia & Co. SPA v. Thurmann-Nielsen*, Lord Denning explained that;

The Seller is entitled, before he ships the goods, to be assured that, on shipment, he will get paid. The seller is not bound to tell the buyer the precise date when he is going to ship; and whenever he does ship the goods, he must be able to draw on the credit... If the buyer is to fulfil his obligations, he must therefore make the credit available to the seller at the very first date when the goods may be lawfully shipped in compliance with the contract.²⁷⁵

The decision of the court is relevant that when the parties failed to specify the time for opening of the credit, it will be at the earliest time before shipment of the goods. Thus, it can fill the gaps in the contract and avoid potential conflicts between the parties.

The application and instruction for issuance of letter of credit should provide details of the credit. Most importantly it needs to contain; the bank with which the credit is available, list of documents that need to be tendered by the beneficiary, the modes of payment and expiry date of the credit. In this regard the Ethiopian Commercial Code did not mention these details of the credit as an obligation of the applicant. If we consult UCP600, however, one can find stipulations that regulate the case in point. For instance, Article 6 of the UCP600 provides that the credit needs to contain; the bank with which the credit is available, list of documents required, the modes of payment and expiry date of the presentation. The important question at this juncture is, what will result if the credit does not contain these details? For instance, what will be the expiry date of the credit, if there is no specification in this regard? As usual our Commercial Code is silent. UCP600 also did not contain rules that can be cited for this purpose. The UCC, however, provides rules that are relevant for the aforesaid issues. Section 5-106 (c) and (d) specifies, if the credit does not contain expiry date, the credit will expire a year after its issuance date. If the credit is issued for 'perpetual', it will expire after five years of its issuance date.

The other most important duty of the applicant in the credit is, the duty to reimburse the issuing bank. Once the issuing bank pays the beneficiary or reimburses the paying correspondent bank, it will have an automatic right of reimbursement against the applicant. However, under the normal course of things it is not the subject matter of letter of credit. It is rather regulated by separate

²⁷⁵ *Pavia & Co. SpA v. Thurmann-Nielsen* [1952] 1 Lloyd's Rep. 153

agreements between the applicant and the issuing bank. As mentioned under article 959 (1) of the Commercial Code, they might agree that goods represented by the documents may be held and disposed by the issuing bank.

3.4.2. Undertakings' of the Beneficiary

Albeit there is no definition in the Commercial Code as to who is the beneficiary, by looking other provisions it is possible to deduce that the beneficiary is a person in whose favor the credit is issued. Similar definition is adopted under Article 2 of the UCP600. The beneficiary in the letter of credit is usually the seller or exporter in the sale contract. The seller has an obligation of delivery of goods having the same quality and quantity as described in the contract and handing over of necessary documents.²⁷⁶ Coming to the case in point, the beneficiary has firm obligation in the letter of credit transaction. One of the most important obligation is shipment of the goods as indicated in the contract. However, this is not a matter that should be regulated under documentary credit laws. It is a matter that should be regulated under the relevant contract laws, specifically sale contract laws.

After shipment of the goods, the beneficiary is required to provide the documents specified in the credit. His submission is subject to two main parameters. One, the documents tendered should be strictly conform to the terms and conditions of the credit. Second, he has to submit these documents in time, before expiry of the date for presentation. However, as I said somewhere else above, our Commercial Code is silent on the date of presentation of documents and expiry of the credit. Regarding the concept and standard of strict compliance and the position of our Commercial Code, *infra Section 3.3 of the study*.

3.4.3. Issuing Bank Undertakings'

No refers of issuing bank is made under the Ethiopian Commercial Code. The code instead calls it as 'the bank opening the credit'. For instance, Article 960 of the Code begins by stating "[t]he bank opening the credit..." The Code opt to give it a unique and somehow long nomenclature than using the most popular one, 'issuing bank'. However, practically these two nomenclatures are one and the same and have no difference as such. The Code apart from naming the bank, it does not define what it is or what it shall be.

²⁷⁶ See the 1960 Commercial Code of Ethiopia, Book V, Chapter 2, Obligations of the seller and see also United Nations Convention on Contracts for the International Sale of Goods (1980, Vienna), Chapter II, Obligations of the seller

The UCP600 define it as “...the bank that issues a credit at the request of the applicant or in its own behalf.”²⁷⁷ Thus, according to this definition issuer of letter of credit is always a bank. Besides, the issuer can issue a credit either at the request of the applicant or through its own initiation.

The UCC, on the other hand, define it as “...a bank or *other person* that issues a letter of credit but does not include an individual who makes an engagement for personal, family, or household purposes.”²⁷⁸ (Emphasis added). The different element in this definition from the UCP600 is that, issuer of letter of credit can be ‘any person’ other than a bank with the exclusion of persons who engages for personal, family or household purposes. With this in mind, are persons other than banks are allowed to issue letter of credit in Ethiopia? There is no statement in the Code which clearly affirm or otherwise prohibit issuance of letter of credit by a person other than a bank. Thus, in order to answer this question we have to resort to other relevant laws.

The Banking Business Proclamation No. 592/2008 did not specifically mention letter of credit operation as a banking business, instead it provides a general reference that banking business includes any activity that are customarily recognized as banking business provided that the NBE authorizes to do so. NBE, in the Directive No. SBB/60/2015, stated that banking business includes any customary banking activities. Now the question will be, is letter of credit operation customary banking activity? Is NBE authorizes banks to operate letter of credit? To answer the first question one can simply refer UCP600 as the rule is an expression of the custom and practice of banks letter of credit operation around the globe. Accordingly article 2 of the rule makes clear that letter of credit is a banking business. In another Directive the NBE stipulated that “Commercial Banks which are licensed to operate in Ethiopia are authorized to allow imports and exports excluding coffee and provide associated services against submission of the required documents by the importer and exporter.”²⁷⁹ It further clarifies that, the import and export transaction should be processed by letter of credit or other payment instruments subject to the restrictions therein.²⁸⁰ Accordingly if we look these provisions constructively, issuance of letter of credit is a banking

²⁷⁷ UCP600, Article 2

²⁷⁸ UCC, Section 5-102 (a)(9)

²⁷⁹ Directive No. FXD/07/1998, Article 4

²⁸⁰ See Directive No. FXD/07/1998, Article 5.1 and 6.3

business in Ethiopia. The Commercial Code's categorization of the instrument in the Chapter titled Banking Transactions also strengthens the aforementioned argument.²⁸¹

The primary obligation of the issuing bank is to receive instructions from the applicant and issue the credit accordingly. As discussed in the beginning of this section, in letter of credit transaction there shall be an agreement between the applicant and issuing bank that the latter will issue a credit according to the contractual agreements.

There is no regulatory provision in the Commercial Code as to the obligation of the issuing bank to receive instructions from the applicant and issue the credit accordingly. Nor conditions of the instructions given by the applicant are regulated in the Code. Besides, the Code is also failed to state the consequences of failure of the issuing bank to issue the credit according to the instructions of the applicant.

The English Court approach this issue in the case *Midland Bank v. Seymour*²⁸² as “[t]he banker is obliged to act upon them [instructions of the applicant] precisely.” To do so, however, the applicant needs to give clear instructions. In the same case, the Court stipulates; “...no principle is better established than that when a banker ... is given instructions..., they must be given to him with reasonable clearness...” The Court reinforces the issue by stating, “...when [the bank] acts upon ambiguous instructions he is not in default if he can show that he adopted what was a reasonable meaning.”²⁸³

Whenever the issuing bank fail to comply with the accepted instructions of the applicant as indicated in the English Case, *Equitable Trust Company of New York v. Dawson Partners Ltd.*²⁸⁴, it may result (1) a breach to the contractual undertaking of the issuing bank or (2) the issuing bank might be denied its right of reimbursement.

The second obligation of the issuing bank is examination of documents submitted by the beneficiary. Article 965 of the Commercial Code specified the obligation of the issuing bank as, “[t]he bank shall satisfy itself that the documents conform strictly to the instructions contained in the credit.” The Code, however, does not state the maximum duration for examination of documents. The UCP600 provides a maximum of five banking days in this regard.²⁸⁵

²⁸¹ The Commercial Code, Book IV, Title III

²⁸² *Midland Bank v. Seymour* [1955] 2 Lloyd's Rep 147

²⁸³ *Ibid*

²⁸⁴ *Equitable Trust Co. of New York v. Dawson Partners Ltd.*, (1927) 27 L.J.L.Rep.49.

²⁸⁵ UCP600, Article 14(b)

The third obligation of the issuing bank is honoring complying presentation made by the beneficiary. Whenever the beneficiary tender documents that strictly conform to the terms and conditions of the credit, the issuing bank will have an undertaking to pay him. Article 960 of the Commercial Code specified that the issuing bank has an obligation to pay, accept, discount or negotiate the drafts drawn by the beneficiary. Indeed, this obligation of the issuing bank also indicated under Article 7 of UCP600. In addition to what are mentioned in the Commercial code, the UCP600 added that, the issuing bank is obliged to reimburse a nominated bank that has honored or negotiate a complying presentation.²⁸⁶

The fourth obligation of the issuing bank is forward the documents to the applicant pending its right of reimbursement against the latter. The Commercial code, however, does not have any rule that can regulate the matter.

3.4.4. Corresponding Bank Undertakings'

As discussed somewhere else above, the fourth important contractual relationship that accompanied letter of credit is a contract between the issuing bank and the Corresponding Bank. The Corresponding Bank sometimes referred as Beneficiary's Bank might serve as conforming bank or advising bank.

The Commercial Code under article 964 (1) states that the conforming bank has a "definite undertaking". However, there is no any explanation in the Code as to what constitutes definite undertaking is. Thus, it will be subject to interpretation of the court. In this regard, looking to the UCP600 provisions are important. Article 8 of the Rule specified that, the issuing bank has an obligation to honor complying presentation by effecting a payment to the beneficiary in one the modalities indicated in the credit. It also obliged to reimburse the nominated bank, if any, that has honored or negotiated a complying presentation. Thus, in terms of honoring complying presentation the conforming bank has an identical obligation to the issuing bank. After payment to the beneficiary, the conforming bank has a right of reimbursement against the issuing bank.

When we come to the advising bank, our Commercial code has a noticeable gap. It failed to incorporate provisions that can regulate rights and obligations of the advising bank. It does not even recognize involvement of the advising bank in the letter of credit operations. This gap of the Code is, indeed, become a cause for controversies among parties involved in the credit. The case

²⁸⁶ Id, Article 7(c)

Grain Trade Enterprise v. Commercial Bank of Ethiopia, is a good example that shows how the code badly lagged behind improvements. In the case, the plaintiff entered into a contract with Pakistani importer, M/S Patel & Co. or Nominee Grain Center, on 02 May 2008. In their agreement the plaintiff will deliver 400 Metric Ton of Chick Peas to the importer and the importer will open irrevocable letter of credit for a price of \$280,000.00. According to their agreement, the irrevocable letter of credit was issued by the Abn Amro Bank (Pakistan) with a credit No. NLNL1NL08E104142. With the request of the issuing bank, the CBE became an advising bank. Then the plaintiff shipped the required goods and tendered the documents to the CBE. The CBE in turn forwarded the documents to the issuing bank. However, the issuing bank rejected the documents by stating that some of the documents are not strictly complied with the terms and conditions of the credit and refused to effect payment upon them. When the plaintiff received such notification, it sue the CBE at the Federal High Court for payment of the price in the credit.

By looking at material facts, the Court frames the issue of the case. That is “what is the responsibility of Commercial Bank of Ethiopia as an advising bank of the credit? One of the main challenges of the case was absence of provisions in the Commercial Code that regulate undertakings of the advising bank. Nothing is mentioned or indicated in the Code as to the advising bank. That is why the issue becomes a point of dispute between the parties

The plaintiff argued that the credit is an irrevocable letter of credit, the defendant that involved in the operation of the credit knows that the credit is irrevocable, thus, it should pay what is indicated in the credit. Whereas the defendant argued that, it does not confirm the credit rather it only assumes the obligation of advising the credit. Thus, it argued that it does not have an obligation to pay the price in the credit.

The court after duly examined the facts of the case and relevant laws, it decided;

As we can see from the facts of the case the defendant does not assume the obligation of conforming the credit. It rather assumes the status of advising bank and nominated bank. By the acontrario reading of Article 964 (1) of the Commercial Code and Article 9 (a) and 12 (c) of UCP600 the defendant does not have an obligation to pay the plaintiff as the advising bank does not have an obligation of honoring complying presentation. Thus, the claim of the plaintiff is rejected according to article 255(1) of the Civil Procedure Coed of Ethiopia.²⁸⁷(See the decision of the High Court in Attachment 3)

²⁸⁷ Grain Trade Enterprise v. Commercial Bank of Ethiopia, Federal High Court, 2008, Civil Case No. 13440 [unpublished]

The plaintiff appealed the case to the Federal Supreme Court. The Supreme Court affirms the decision of the Federal High Court ²⁸⁸(see the decision of the Supreme Court in Attachment 4). The plaintiff again made an application to the Federal Supreme Court Cassation Division. The Cassation Bench reaffirms the decision made by the High Court and Supreme Court by arguing that the obligation of the advising bank is limited to advise the credit and check its apparent authenticity (see the decision of the Cassation Bench in Attachment 5).²⁸⁹

3.5. Electronic Letter of Credit under the Ethiopian Legal Framework

Relevant section of the Ethiopian Commercial Code begins with caption of “*Documentary Credit*” and the Amharic version with “*በሰነድ ሰለጣኒ ሰጠው ብድርጅቻ*”.²⁹⁰ Both versions of the caption emphasis on documentary natures of the credit. If we look at the defining provision, Article 959, it again makes a special emphasis on inevitable involvement of documents under letter of credit transactions. In its wording, “documentary credit is opened by a bank providing payment against *presentation of specified documents...*” (Emphasis added). The same emphasis on ‘submission of documents’ in the credit is endorsed under article 963, 994(4), 995 and 996 of the Code. Apart from the Commercial Code, the NBE of also specified the need for submission of documents for both import²⁹¹ and export²⁹² letter of credit transactions.

Thus, the most important issue that worth discussing is, does the definitional reference, in Article 959 and other related provisions, to the instrument as “document” restrict the ability of Ethiopian letter of credit law to accommodate itself to future developments toward paperless (electronic) letter of credit? In order to properly answer this question we have to look first the definition of document.

Black’s Law Dictionary defines document as;

Something tangible on which words, symbols, or marks are recorded. The deeds, agreements, title papers, letters, receipts, and other written instruments used to prove a fact.²⁹³

In another instrument it is defined as “...written or writing includes printing, typewriting or any intentional reduction to tangible form.”²⁹⁴

²⁸⁸ Grain v. Commercial Bank Trade Enterprise of Ethiopia, Federal Supreme Court, 2008, Civil Case No. 104049 [unpublished]

²⁸⁹ Grain Trade Enterprise v. Commercial Bank of Ethiopia, Federal Supreme Court Cassation Division, 2010, Civil Case No.123162 [unpublished]

²⁹⁰ The Commercial Code, Book IV, Title III, Chapter 5, Section 4

²⁹¹ Directive No. FXD/07/1998, Article 4 and 5.1

²⁹² Id, Article 4 and 6.6

²⁹³ *Black’s Law Dictionary*, 8th ed., s. v. “document”

²⁹⁴ UCC, Section 5-103(1) (b)

As we can understand from these definitions, document is associated with paper and written instruments, thus, it excludes paperless or electronic records. Due to development of technologies, electronic records of computers, telephones, and artificial satellites are used for business dealings in general and letter credit transactions in particular. Communication among banks, significantly, become paperless, such as through Society for World Wide Inter-bank Financial Telecommunication (Herein after SWIFT).²⁹⁵ Similarly, communication of letter of credit through electronic records to the beneficiary is increased sharply. Currently, it gets large volume and worldwide scope.²⁹⁶ In response to this, the ICC drafted and published the eUCP as a supplemental document to UCP600. It came into effect on April 1, 2002. However, it will be applicable if and only if the parties expressly agree as to its application.²⁹⁷ Besides, Despite eUCP is supplementary document of UCP600, agreement of the parties for application of the latter cannot render the application of the former.²⁹⁸

According to Article e3(b) of eUCP, any electronic records such as; data created, generated, sent, communicated, received or stored by electronic means can establish a credit or called therein as far as they are capable of being authenticated and examined for compliance. The unique aspect of eUCP is that, it allowed presentation of electronic records alone or in combination with paper documents, if the parties agree to do so.²⁹⁹

The UNCITRAL also issued the Model Law on Electronic Commerce, including letter of credit transactions, with the view to be a temple for national legislations.³⁰⁰ The UNCITRAL apart from preparing a model law, it also encourage countries to recognize electronic letter of credit by stating its official view of;

[E]lectronic records can provide the same level of security and in most cases, a much higher degree of reliability and speed, especially with respect to the identification of the source and content of the data³⁰¹

Expansion of electronic letter of credit across the World, indeed, pressure Ethiopian Banks to launch and increase their electronic letter of credit operations. The CBE and some other banks

²⁹⁵ Boris Kozolchyk, 'The Paperless Letter of Credit and Related Documents of Title', *Law and Contemporary Problems*, 1992, Vol. 55: No. 3, pp. 40-101, at pp. 39-40

²⁹⁶ Id, p. 40

²⁹⁷ eUCP, Article e1 (b)

²⁹⁸ eUCP, Article e2 (a)

²⁹⁹ eUCP, Article e2 (c)

³⁰⁰ UNCITRAL Model Law on Electronic Commerce Guide to Enactment with 1996 with additional article 5 bis as adopted in 1998, at <https://www.uncitral.org/pdf/english/texts/electcom/05-89450_Ebook.pdf> [Last accessed 16 May, 2018]

³⁰¹ Id, p. 20

launched Hi-tech (electronic) letter of credit some years before.³⁰² Besides, currently, communication of Ethiopian banks with foreign banks successfully become electronic, esp. through SWIFT.³⁰³

Despite the introduction and increment of electronic letter of credit transactions in Ethiopia, there is no legal rule that regulates such transactions. Documentary Credit provisions of the Commercial Code of Ethiopia are totally incompetent to regulate these transactions. Its persistent refers to “documents” and absence of flexibility to include electronic records makes the Code irrelevant to electronic letter of credits. Electronic signature, retention of electronic records, their evidentiary value (admissibility, relevancy and weight), and liabilities in case of fraud in the network are matters that badly faced dearth of legal rules in Ethiopia. Thus, it is needless to say that legal rules are needed that can effectively regulate the subject matter. In response to this, INSA prepared a draft rule of electronic commerce that includes electronic letter of credit transactions. The promulgation of the draft may solve this problem, provided that the draft is comprehensive enough to comprehend matters that encompass electronic letter of credit transactions.

³⁰² Interview with Zelalem Asmare, Manager of International Banking Department at Hibret Bank, on *the import and export letter of credit operation in Ethiopia*, 3 April 2018.

³⁰³ Ibid

CHAPTER FOUR

BANKING PRACTICE AND MAJOR CHALLENGES OF LETTER OF CREDIT OPERATION IN ETHIOPIA

4.1. Banking Practice of Letter of Credit Operation in Ethiopia

4.1.1. Level of Letter of Credit Operations in Ethiopia

Import and export trades are the backbone to the Ethiopian economy. Due to different capabilities and specialization on production of goods and services no country, including Ethiopia, is self-sufficient, thus, they are highly interdependent of one another.³⁰⁴ That makes import and export transactions across national boundaries very common and indispensable phenomenon since the time of immemorial.

The level of import and export transactions in Ethiopia are increasing from time to time. According to the report of NBE, Good's export of Ethiopia reached \$2.8 Billion in the 2016/2017 Annual year.³⁰⁵ The main export commodities were Coffee (29%), Oil seeds (19%), Gold (11%), Chat (10%), Pulses (9%), Flower (9%), Leather and leather products (5%) and others (8%).³⁰⁶ The exports were mainly destined to Asia (37.7%), Europe (32.4%), Oceania (21.5%), America (7.5%) and Africa (0.9%).³⁰⁷

The import transactions of Ethiopia also increased significantly and reached \$15.6 Billion in the 2016/2017 Annual Year.³⁰⁸ The main import items were Capital Goods (38.2%), Consumer Goods (31.0%), Semi-finished goods (16.6%), Fuel (11.5%), Raw Materials (0.8%) and others (1.9%). These items are mainly imported from Asia (62.65%), Europe (22.5%), America (7.8%), Africa (5.2%) and Oceania (0.11%).³⁰⁹

According to the Directive of NBE, all import and export transactions should be processed by Commercial Banks authorized to operate in Ethiopia.³¹⁰ The NBE provide different modalities of

³⁰⁴ G. V. Vijayasri, 'The Importance of International Trade in the World', *International Journal of Marketing, Financial Services & Management Research*, 2013, Vol.2, No. 9, pp. 111-119, at p. 112

³⁰⁵ National Bank of Ethiopia, Annual Report 2016/17, p.46-57

³⁰⁶ Id, p.77

³⁰⁷ NBE, 2016/2017 Annual Report pp.47-48

³⁰⁸ Id, p.50

³⁰⁹ Id, p.51-53

³¹⁰ Directive No. FXD/07/1998, Article 4

payment for import³¹¹ and export³¹² transactions. However, for different reasons options of the traders to use the instruments of their choice is restricted by the NBE. For instance, it specified that foreign exchange approval for import and export payment shall only be on the basis of letter of credit.³¹³ In addition, any import and export transaction more than \$5000 should only be processed through letter of credit or cash against document.³¹⁴

The informants from some of the commercial banks³¹⁵ revealed that majority of import and export transactions in Ethiopia are processed via letter of credit than other instruments. This is basically caused by two main factors. The first is associated with the nature of the instruments other than letter of credit say cash against document. Compared to letter of credit, they are less secured modes of payment, they are usually used by traders who have trust to each other. When we look at the reality of trade across national boundaries traders are anxious on the possible risks, hence, they usually demand the highly secured mode of payment, typically letter of credit. The other reason is connected with the commercial reality of the world. In the business community of the world, letter of credit is considered as “the life blood of international commerce.”³¹⁶ As letter of credit is the commercial instrument used to finance import and export transactions all over the world, the Ethiopian traders and bankers would not have choice (at least in the business sense) to replace it by other commercial instruments. The statement of NBE also affirms that letters of credit are the most widely used instrument to finance foreign exchange in Ethiopia.³¹⁷

If we take CBE as example thousands of letter of credits and millions of dollars are transacted within few months.³¹⁸ One can imagine the amounts of letter of credits transacted in the whole eighteen banks in a year. The amount of letter of credit transactions across eighteen commercial

³¹¹ Payment instruments that can be employed for import transactions are letter of credit, cash against document, advance payment, Franco-Valuta and suppliers' credit. See Articles 5.1, 5.3, 5.4 and 5.8 of Directive to transfer NBE's Foreign Exchange Functions to Commercial Banks Directive No. FXD/07/1998

³¹² Payment instruments that can be employed for export transactions are letter of credit advance payment and consignment. See article 5.3 Directive to transfer NBE's Foreign Exchange Functions to Commercial Banks Directive No. FXD/07/1998

³¹³ Directive No. FEC/43/97, Article 2

³¹⁴ Directive No. FXD/07/1998, Article 5.4 cum 5.3 and 5.1

³¹⁵ Interview with Ato Anteneh Girma, Manager of Credit Service Central Processing Unit at Commercial Bank of Ethiopia, on *letter of credit operation in the Ethiopian Banking Practice*, 5 March 2018

³¹⁶ Zsuzsanna, *Documentary Credits in International Commercial Transactions*, p. 17

³¹⁷ National Bank of Ethiopia, *Bank Risk Management Guidelines (Revised)*, 2010, p. 41

³¹⁸ Lubaba Mohammed *et al*, *An Assessment of Letter of Credit in Import and Export Case of Commercial Bank of Ethiopia*, Senior Essay, St. Mary's University, Faculty of Business, 2014, p .35

banks in Ethiopia are sufficient enough to attract the attention for critical examination of the banking practice in order to identify the major challenges and propose appropriate solutions.

4.1.2. Letter of Credit Issuance Procedure in Ethiopia

In Ethiopian banking practice letter of credit is categorized into import letter of credit and export letter of credit. However, this classification is only for practical purpose and has nothing to do with the types of the letter of credit. Because, it is that same letter of credit possess both import and export credit viewed from two opposite sides of the importer and the exporter. The Ethiopian banks handle letter of credit operations through their International Banking or Trade Service Departments. All commercial Banks have their own internal letter of credit procedures, usually named as Foreign Bank Operation Rule/Procedure/Manual or Trade Service Procedure.³¹⁹ These procedures are enacted to implement the international banking operations policy, institute uniform and standard trade service practices across all branches of the bank, guide performers in their day-to-day activities of rendering services and ensure operational consistency and adherence to uniform trade service practices.³²⁰ These procedures are usually referred as governing rules in letter of credit transactions by the bank.

Banks usually specified general eligibility criteria for traders who wants to import or export goods through letter of credit.

Generally bankers open letter of credit for customers who open and maintain an account with the bank. NBE specified mandatory requirements for imports by letter of credit.³²¹ The applicant first needs to submit duly completed, signed and stamped foreign exchange application form for imports to the respective bank. Once the importer secured foreign exchange permit, he needs to submit it with the application form. Practically, banks supply printed formats to the applicants, hence, they only needs to fill all details properly and sign them (see the application form in Attachment 1). In addition to the application form, the importer is required to provide insurance certificate from licensed local insurance company that will serve as a guarantee to the issuing bank.³²²

³¹⁹ For example, Hibret Bank promulgate “Foreign Banking Manual, United Bank Share Company. -IBD, 2015.” Cooperative Bank of Oromia enacted “Import and Export letter of credit procedure of Cooperative Bank of Oromia.” Development Bank enact “Development Bank of Ethiopia International Banking Service Procedure” and Commercial Bank of Ethiopia prepare

³²⁰ Commercial Bank of Ethiopia, Trade Service Procedures, Section 1.2

³²¹ Directive No. FXD/07/1998, Article 5.1

³²² Id, Article 5.1(d)

The applicant also required to submit proforma invoices³²³ showing clearly full description of the goods³²⁴ along with name and address of the beneficiary and advising bank, the types of letter of credit, the amount to be payed and its source, expiry date of the credit and the documents required. The documents practically required in import letter of credit in Ethiopia are; commercial invoice, manufacturer invoice, packing list, transport documents, insurance certificate and bill of exchange.³²⁵

Import license is mandatorily required for opening letters of credit to import goods in Ethiopia. Accordingly, he needs to submit valid trade licenses for foreign trade, investment or industry.³²⁶ There are special restrictions, however, on importation of some specified goods.³²⁷ In such a case, the goods should be specifically indicated in the trade license issued in accordance with Article 17(2) of Federal Government Commercial registration and Licensing Council of Ministers Regulation No.67/1997.³²⁸ In addition to the trade license he have to have a Tax identification Number (TIN) or TIN exemption certificate or letter.³²⁹

At the end the importer is required to provide Clearance certificate from NBE that he has settled his outstanding's.³³⁰ In other words he needs to submit a clearance that he is not listed as a delinquent by the NBE.

When the bank receives duly completed, signed and sealed application from an importer who satisfy all the eligibility requirements, the bank will vet the documents and ascertain the consistency between the documents attached, specifically, the amount of the credit, applicant's name, beneficiary's name, description of goods and etc. In case the credit is opened for margin paid amount less than 100%, there shall be always an approval from the appropriate authority of

³²³ Id, Article 5.1(b)

³²⁴ The description should be comprehensive enough that at least describes quantity, grade, quality, volume, measurement, weight, mode of shipment, terms of payment, unit and total price of the goods at a named place of delivery

³²⁵ Interview with W/rit Almaz Mengstu, Customers Relation Officer at Wegagen Bank, on *the overall letter of credit operation in Ethiopia*, 4 April 2018

³²⁶ Directive No. FXD/07/1998, Article 5.1 (c)

³²⁷ coffee; pharmaceuticals or veterinary medicines; medical appliances; forestry products, wild animals and birds, agricultural, industrial and construction machinery, mechanical appliances and motor vehicles, minerals, chemicals, petroleum and petroleum products; and other goods for which a certificate of competence must be obtained from the pertinent government institution, in order to prevent damage to public health, safety and the national economy.

³²⁸ Directive No. FXD/07/1998, Article 5.2

³²⁹ Interview with W/ro Aster Alemu, Customers Relation Officer of Trade Service at Commercial Bank of Ethiopia, on *the overall letter of credit operation in Ethiopia*, 2 April, 2018

³³⁰ Directive No. FXD/07/1998, Article 5.1 (e)

the bank.³³¹ Besides, the bank will ascertain all relevant charges and commissions are collected as per the term and tariff of the bank.³³²

Finally, the bank issuing the credit will assign the corresponding bank based on indications of the importer. If the importer has no particular preference of any bank the credit will be advised by a bank at the choice of the issuing bank. At the end, the credit will be opened with a specific digital identification numbers and will be send to the beneficiary's bank for advice, (see letter of credit sample under Attachment 2).³³³

Export letter of credit, on the other hand, is incoming letter of credit received by Ethiopian Banks from its overseas correspondent banks for the export of goods from Ethiopia to overseas importers. Thus, unlike import letter of credit, export letter of credit is not something that can be issued or opened by Ethiopian Banks. The Ethiopian banks will involve in the operation if a request for advice or confirmation of the credit is forwarded by the issuing bank (importer's bank).

An Ethiopian bank that receives a request for advising the credit may decide to advice or reject the request. If it decide to advice the credit, as an initial stage, the bank will check the authenticity and go through the text and ascertain that the credit is issued in line with ICC publication, NBE directive and the bank's rules and procedures.³³⁴ At this point, a key informant revealed that they never consulted the Commercial Code.³³⁵ If the credit is as per the standard, advise beneficiary with formal covering letter against the recipients' signature. If the credit is not in compliance with the above rules and regulations, immediately advise to the issuing bank and to the exporter for the necessary correction and subsequent amendments. If the credit is unauthenticated or bears unacceptable terms and conditions, which cannot be corrected, return the credit officially to the issuing bank stating the reason for rejection of the credit.

The NBE stipulates documents that are necessary for payment under export letter of credit, though it is mainly for the purpose of foreign exchange regulation. At first the exporter needs to have foreign trade license. In addition, if the goods are under the list of restricted goods³³⁶, there needs

³³¹ Interview with W/ro Meklit Bekele, Assistant Manager Trade Finance Department at Hibret Bank, on *the practical operation of letter of credit*, 4 April 2018

³³² Interview with Ato Moges Dero, Senior Credit Analyst officer at Hibret Bank, on *import and export letter of credit operation in Ethiopia*, 4 April, 2018.

³³³ Ibid

³³⁴ Ibid

³³⁵ Interview with Ato Alebacew Fasil, Loan and Trade Finance Customers Relation Officer at Oromia International Bank, on *the types of letter of credit used in the Ethiopian Banking practice*, 3 May 2018

³³⁶ The restricted goods are listed under Article 6.6 (b) of Directive to transfer NBE's Foreign Exchange Functions to Commercial Banks Directive No. FXD/07/1998. The goods include; Forestry products, wild animals and birds,

a special trade license that specifically indicate the goods required.³³⁷ Apart from the trade license, the exporter is required to submit authenticated letter of credit, customs declaration, bank declaration, sale contract and commercial invoices.³³⁸

When the exporter present documents for payment under the credit the bank will ascertain that all documents called upon in the credit are presented and examine their conformity to the terms and conditions of the credit. Among the documents, bill of lading has to be issued to the order of the advising bank and endorsed to the issuing bank or directly issued to the order of the issuing bank. In other word, bill of lading should not be issued to the order of the importer and exporter.³³⁹ The bank will continue to advice the credit until the complying presentation of the exporter is honored or otherwise rejected by the issuing bank for non-compliance or some other reasons.

Another aspect related to export letter of credit is adding confirmation in it. Confirmation can be at the request of the issuing bank or by the initiation of the conforming bank itself usually referred as silent confirmation. Unfortunately, the Ethiopian banking practice is unsatisfactory in this regard. Banks does not provide detail procedures as to the process of confirmation. They usually hesitate to conform export letter of credits.³⁴⁰At this point it has to be noted that, conforming the credit cannot provide liability if it handled diligently. Of course, providing a service of conformation of a credit is also obligation of banks as far as they are engaged in banking businesses. The Directive of NBE also affirms this stand by stating, “[c]ommercial banks shall allow exports for goods to be exported abroad on irrevocable and/or confirmed letter of credit basis.”³⁴¹ Apart from that, it is good business for the banks as they can earn significant amount of commission for the service of confirmation. Equally so, it is important for the Ethiopian exporters as confirmation provide additional guarantee for payment. Thus, the trends need to be corrected.

minerals, other goods for which a certificate of competence must be obtained from the pertinent government institution in order to prevent damage to the public health, safety and the national economy.

³³⁷ Directive No. FXD/07/1998, Article 6.6(A)(a)

³³⁸ Id, Article 6.6(A)(b)-(f)

³³⁹ NBE, 1995, National Bank of Ethiopia, Exchange Control Notice to Exporters on Documentations Regarding shipments Abroad Public Notice No. 32/95, 21 August 1995, Section 1

³⁴⁰ Interview with W/rit Almaz Mengstu, Customers Relation Officer at Wegagen Bank, on *the overall letter of credit operation in Ethiopia*, 4 April 2018

³⁴¹ FXD/26/2004, National Bank of Ethiopia, Amendment to Directive No. FXD/07/1998, 01 January 2005, Article 6.7(b)

4.2. Major Challenges of Letter of Credit Operation in Ethiopia

4.2.1. Problems Due to Fraud in Letter of Credit

One of the major problem facing letter of credit operation in Ethiopia is documentary fraud. As discussed in chapter three of the paper, letter of credits are independent of the underlying contract conclude between the parties and the credit agreement between the issuing bank and the applicant. The credit is disassociated with the actual performance of contracts accompanying it. Thus, when banks measure compliance of documents it should restrict itself to the terms of the credit and the documents presented. This principle no doubt promotes the smooth operation of letter of credit. However, an absolute separation of the credit from the actual performance of the contract creates ample opportunity for fraudsters to abuse the system. That makes fraud the major threat to the international trade

Common types of frauds are issue of forged bills of lading, insurance policies and commercial invoices. The first instance is falsification of cargo documents while no goods are in fact shipped. In collusion with shipping companies, shippers and insurers forged cargo documents are prepared for payment in the credit while in fact no good is actually shipped. The other instance is when forged commercial invoices, cargo documents and insurance certificates are submitted for goods that are actually inferior in terms of its quality and quantity to what the documents denoted. It also happens that fraudulently the same goods are sold to two or more persons and same cargo documents are issued twice for the same merchandises.³⁴²

At this point one might ask the volume of fraud experienced in the Ethiopian import and export transactions. Thousands of letter of credits and billions of dollars are transacted in Ethiopia through its banks. It is logical that the more international commercial transactions the more issues related with letter of credit in general and fraud exception in particular. To the writer's dismay, however, there is no official records either in the banks or NBE that shows the exact number of letter of credit fraud in Ethiopia. However, its existence is undeniable. As a key informant revealed fraud in bill of lading documents are frequently experienced. He added that, forged cargo documents are issued for goods that are not shipped or for goods that are inferior to what is indicated in the cargo.³⁴³ However, bankers and traders are not volunteer to disclose such and the like fraud

³⁴² Interview with Ato Melaku Mekonen, Manager of Legal Service Division at Ethiopian Shipping and Logistic Service Enterprise, on *the issue of Fraud relating to bill of lading in letter of credit transactions*, 4 April 2018

³⁴³ Ibid

situations as they justify it with protecting customer's information and indeed, some of the fraud cases are interlinked with corruption scandals relating to foreign exchange.³⁴⁴

Most of the time fraud in letter of credit are left unnoticed to the public. It comes to light only when one of the parties raises dispute. In this regard the experience of *Yeju Honey and Honey products Processor PLC (importer)* with the Indian Exporter named, *Filtron Limited* is mentionable. The parties enter into an agreement in 2013 for machine design, production and installation with the price of €214, 180.00 payable through irrevocable letter of credit. However, in breach of the contractual obligation, the exporter deliver incompatible and second-hand machineries while it receive the payment by submitting forged bill of lading and commercial invoice documents. The attempt by the Ethiopian importer to enjoin the payment by requesting the issuing bank (CBE) was fruitless. Due to this, the Ethiopian importer incurred significant losses of 11,260,066.79 birr.³⁴⁵

In another case, The Reporter unveils a case of forgery of letter of credit to unduly transfer money. A defendant named *Micheal Maston* and *Aimen Abdela* charged by the public prosecutor for forgery of letter of credit, specifically the defendants allegedly prepared overvalued forged bill of lading and commercial invoices for payment in the credit. With the instrumentally of these forged documents they unduly derive 62.3 million birr from CBE.³⁴⁶

There are also cases where forgery of documents are involved in letter of credit transactions by preparing over invoiced imports and under invoiced exports in order to unduly obtain excessive foreign exchanges and avoid tax liabilities respectively.³⁴⁷ This problem is noticed by the public authorities of NBE, ERCA and the Ministry of Trade. They are indeed in the verge of forming a joint taskforce to verify the actual approved letter of credit and the value of import items.³⁴⁸

The problem is worsen because of absence of any law that regulated fraud exception. As dealt earlier, UCP from its inception in 1929 to its latest version of UCP600 did not incorporate rules for fraud exception. It is permanent perception of the ICC that, the matter should be handled by

³⁴⁴ Yewondwossen, M., 'The role of National Bank of Ethiopia in foreign currency allocation', *The Ethiopian Herald*, 2015, Vol. 6, p.23

³⁴⁵ Interview with Tegegn Zergawu, Former Legal Compliance Expert of Tired Corporate, on *the issue of letter of credit fraud in Ethiopia*, 8 April 2018

³⁴⁶ The Reporter, *Two Foreigners Charged with Forex Fraud*, at <<http://archiveenglish.thereporterethiopia.com/content/two-foreigners-charged-forex-fraud>> [last accessed at 19 May, 2018]

³⁴⁷ Eyader Teshome, *Legal and Regulatory Issues of Ethiopian Currency (Foreign) Exchange Regime and Transactions*, LLM Thesis, Bahir Dar University, School of Law, 2017, p. 97 [Herein After Eyader, *Legal and Regulatory Issues of Ethiopian Currency (Foreign) Exchange Regime and Transactions*]

³⁴⁸ Ibid

national laws. Unfortunately, Ethiopia is not yet enacted fraud exception rules either in the form of proclamation, regulation or directives. Due to this banks are not willing to enjoin payment though fraud in the credit is claimed by the innocent party. They usually justify that, they do not have statutory mandate and obligation to do so and they do not want to compromise their reputation in the international commerce by engaging in such activities.³⁴⁹

4.2.2. Problems due to Discrepant Documents in Letter of Credit

As we have discussed under chapter three of the paper, strict compliance is one of the important principles of letter of credit. It dictates that documents presented by the beneficiary should strictly conform to the terms and conditions of the credit and relevant legal rules. The Commercial Code as well as ICC rules recognize the principle of strict compliance. Therefore, banks should assure the conformity of the documents to the required standard. However, this does not mean banks should reject documents for each and every irrelevant discrepancy.

The banking practice in Ethiopia is not uniform in this regard. Some banks adopt procedure that, when documents are found discrepant, the first task will be advising the exporter for correction of the documents than rushing to communicate the matter for the issuing bank or the applicant. If that is corrected as intended, there will not be an issue of negation of discrepancy and payment of discrepancy fee. Some other banks, on the other hand, does not have such procedure, thus, every discrepancy will go through the negotiation process.³⁵⁰

When we come to advising discrepant documents there is noticeable differences among banks. Some of the banks such as Hibret Bank and Development Bank have a practice of classifying discrepancies into major and minor. When there is major discrepancy the first procedure the banks adopted is that, list the discrepancies noted and advice the applicant (importer) by using the format designed for this purpose. The same will be communicated to the issuing bank though SWIFT. The discrepancies will be exempted if and only if the applicant waive the discrepancies with written and signed letter. However, when the discrepancies are minor, there is no need to go through these time taking procedures. Thus, simply payment will be effected by the bank against indemnity agreement signed by the exporter.³⁵¹

³⁴⁹ Interview with W/ro Aster Alemu, Customers Relation Officer of Trade Service at Commercial Bank of Ethiopia, on *the overall letter of credit operation in Ethiopia*, 2 April, 2018

³⁵⁰ Interview with Ato Ferid Bedru, Customers Relation Officer of International Banking Department at Hibret Bank, on *the import and export letter of credit operation in Ethiopia*, 5 March, 2018

³⁵¹ Foreign Banking Manual, United Bank Share Company. -IBD, 2015, Section 2.4

Some other banks, however, does not have such kinds of classification of discrepancies. Thus, every discrepancies, though immaterial, has to go through very stringent procedures. That is without a doubt time taking and my last for many days, which may result expiry of the credit due to lapse of time.

It has to be noticed that, the banks have a duty to ascertain compliance of documents. Equally so, the bank should not consider every silly error and misspelling as non-compliance. An informant revealed that, in our banking practice discrepancy is not only a problem but a business too, as banks always charge \$50 or its equivalent fee for each presentation of discrepant documents.³⁵²

4.2.3. Problems due to Time Limits of Letter of Credit

It is accepted view that reasonable time has to be fixed for any commercial activities. As well-known letter of credit is an international payment instrument that has to pass through plenty bureaucracies of different jurisdictions. The issue will be better explained with an illustration. Assume an Ethiopian exporter enter into an agreement with the Chinese importer for delivery of goods that are manufactured by Sudanese supplier. Thus, in order for the Ethiopian exporter to get paid with the credit he will be obliged to go through all the bureaucracies there in Sudan and here in Ethiopia. Besides, the documents required in letter of credit are very technical and principally they should be issued by different authorities. Thus, letter of credit operation should be arranged with sufficient time gap. Equally so, an extended or unbound time should not be set in letter of credit operation as it will be dangerous as equal as denying any time. Therefore, stipulating balanced reasonable time is at the heart of the transaction.

Looking at the banking practice in Ethiopia, the expiry date for letter of credit is three months (90 days) from its time of issuance.³⁵³ NBE also provided that an Ethiopian exporter is required to repatriate the proceeds (usually paid through letter of credit) of foreign exchange within 90 days from the date of issue of export applications.³⁵⁴ Ethiopian importers, besides to expiry of the credit within 90 days, are required to submit evidence for the entry of goods into the country within 120 days from the date of issue of import permits.³⁵⁵ At this juncture, it is wise to ask that, are these periods of time reasonable enough? Does these periods of time fair enough to comply the letter of

³⁵² Interview with Ato Ferid Bedru, Customers Relation Officer of International Banking Department at Hibret Bank, on *the import and export letter of credit operation in Ethiopia*, 5 March, 2018

³⁵³ Interview with W/ro Aster Alemu, Customers Relation Officer of Trade Service at Commercial Bank of Ethiopia, on *the overall letter of credit operation in Ethiopia*, 2 April, 2018

³⁵⁴ Directive No. FXD/07/1998, Article 7.1

³⁵⁵ Id, Article 7.2

credit operation for all types of import and export transactions? To the writer's view the period of time sets both in the banking practice and Directive of NBE are not reasonable. One can simply think two exporters the one who export 100 kg teff and the other who export thousands of complicated machineries. Having in mind the difference between these two exports fixing the same 90 days for both of them is unreasonable and unrealistic.

The matter is more exacerbated because of the consequences attached for failure to adhere in the specified time limits. For instance, in the first scenario, if the beneficiary of the credit failed to submit all documents that are strictly conform to the standards required he will forfeit his right to claim in that credit. Practically, the beneficiary (exporter) will have nothing but two undesirable choices. One, request his importer for amendment of the credit. If the importer agree, the credit will be amended for extra time. But still, the parties will be exposed to amendment costs that is actually significant amount of money. Second, if the applicant is not willing as to the amendment, the beneficiary needs to institute a suit against the importer based on the underlying contract. However, this choice is even the worst as it will put the beneficiary at great uncertainty due to the distance between the parties, difference in jurisdictions and legal systems.

In the second scenario, if both the exporter and importer failed to adhere in the 90 and 120 days respectively, they will be categorized in the delinquent list of NBE. The consequence is that, no permit will be given to a prospective exporter or importer (in whatever payment instrument, including letter of credit) whose name appears on the delinquent list until he clear his outstanding commitment at the NBE.³⁵⁶

Stipulation of time limit with no doubt promotes transparency in import and export transactions. However, specification of short time equally hampers import and export transactions in general and operation of letter of credit in particular. Thus, it is advised that, reasonable periods of time need to be set. The period of time should consider, among other things, the difference among various types of imports and exports, the country where the import originates or the export destines, the types of payment instruments applied and the like.

³⁵⁶ Id, Article 7.3 and 7.4

4.4.4. Problems due to Absence of effective individual compliant redress mechanisms

Several individual complaints are made against letter of credit operations of banks.³⁵⁷ The first that needs to be mentioned in this regard is discriminatory allocation of forging exchanges in letter of credit operations.

Shortage of foreign exchange accompanied with depletion of national reserve create a major threat to the import and export transactions in Ethiopia. It causes, among other things, an excessive delay in import and export letter of credit operations. The problem of shortage is exacerbated due to discriminatory allocation, undue delay, corruption and artificial scarcity existed in the foreign exchange market of commercial banks.³⁵⁸ To tackle these problems NBE enacted directive on Transparency in Foreign Currency Allocation and Foreign Exchange Management Directives No. FXD/45/2016.³⁵⁹ The Directive, however, failed to ensure sound and transparent, that is free from corruption and malpractice, foreign exchange allocation as intended. Due to that it ends up repealed and replaced by Directives No. FXD/46/2017.³⁶⁰

The new directive did not list out persons who are/who are not entitled to buy forging exchange from banks. Instead, it come up with some measures that are believed to be a better approach to ascertain transparency in foreign exchange allocation. The first one is, it specified priority in allocation of foreign exchanges for importation of some essential items and payments.³⁶¹ Second, it devised a standard of “first come first served” to select among these who are in the priority list.³⁶² Third, it introduce foreign exchange sale on demand for certain category of persons engaged in the specified activities.³⁶³ These group of persons are exempted from registration and they will be served the foreign exchange on demand. Fourth, as a measure to ensure transparency, it prohibits some conducts of banks³⁶⁴ and importers.³⁶⁵

³⁵⁷ Interview with Aduagna Amaha, Foreign Exchange Inspector at National Bank of Ethiopia, on *the malpractices relating to letter of credit operations in Ethiopia*, 3 April 2018

³⁵⁸ Eyader, *Legal and Regulatory Issues of Ethiopian Currency (Foreign) Exchange Regime and Transactions*, p. 98

³⁵⁹ FXD/45/2016, National Bank of Ethiopia, Directive on Transparency in Foreign Currency Allocation and Foreign Exchange Management, Directives No. FXD/45/2016

³⁶⁰ FXD46/2017, National Bank of Ethiopia, Directive on Transparency in Foreign Currency Allocation and Foreign Exchange Management Directives No. FXD/46/2017, 20 March 2017. [Herein After Directives No. FXD/46/2017]

³⁶¹ Id, Article 6.1

³⁶² Ibid

³⁶³ Id, Article 6.2

³⁶⁴ Id, Article 7

³⁶⁵ Id, Article 11

The directive is highly criticized for being unduly lenient for some kinds of imports and payments with the expense of other importers and exporters.³⁶⁶ It is also noted that, the directive did not bring the objectives it intended to achieve. Specifically, discriminatory allocation, malpractice and corruption are still major constraints in Ethiopian foreign exchange allocations.³⁶⁷

Several complaints also made on daily basis pertaining to problems on excessive delay and malpractices in letter of credit operations.³⁶⁸ Despite these problems, there is no effective individual complaint redress mechanism within or outside the scheme of NBE.³⁶⁹ Thus, the enormity of the problem will remain until an appropriate solutions are devised.

If we look at the experience of some countries such as New Zealand, Australia, United Kingdom and India in this regard, they establish Banking Ombudsman Scheme. In India, for instance, the Banking Ombudsman was first introduced in 1995. Its establishment is revised several times, in 2002, 2006, 2007 and 2009, to establish an effective customer compliant settlement mechanism.³⁷⁰

The Banking Ombudsman is a senior officer who is appointed for a term not exceeding three years by the Reserve Bank of India to redress grievance of customers' against errant banks.³⁷¹ It has the duty to consider individual complaints received relating to banking services, including letter of credit operations. After a due investigation of the matter, it will resolve the problem either by agreement, making recommendations or by awarding the injured party. It also have the mandate and the duty to impose penalties against the perpetrator banks.³⁷²

4.4.5. Problems due to Lack of awareness

In the current complicated and globalized world knowledge is considered as wealth to the organizations and a key factor for success.³⁷³ Knowledge gaps in in crucial sectors such as import and export transactions and their payment systems are holding back some firms from trading the world.³⁷⁴

³⁶⁶ Eyader, *Legal and Regulatory Issues of Ethiopian Currency (Foreign) Exchange Regime and Transactions*, p. 104

³⁶⁷ Ibid

³⁶⁸ Interview with Aduigna Amaha, Foreign Exchange Inspector at National Bank of Ethiopia, on *the malpractices relating to letter of credit operations in Ethiopia*, 3 April 2018

³⁶⁹ Eyader, *Legal and Regulatory Issues of Ethiopian Currency (Foreign) Exchange Regime and Transactions*, p. 104

³⁷⁰ Yogesh Kolekar, Role of Banking Ombudsman in Banking Reforms, 3rd *One Day International Conference on "Contemporary issues in Commerce, Economics and Management"* Monday, 19th December, 2016, p. 4

³⁷¹ Id, p. 3

³⁷² Susmitha, *Documentary Credit Law*, p. 290-291

³⁷³ Elsa Getnet, *Assessment on Causes of Delay in Managing International Banking Transaction: The Case of Lion International Bank S.C.*, Senior Essay, St. Mary's University, Business Faculty, Department of Management, 2014, p. 20 [Herein after Elsa, *Assessment on causes of delay in managing International Banking Transaction*]

³⁷⁴ Id, p. 22

As letter of credit is an international payment instrument in import and export transactions across national boundaries, its commercial aspect and regulatory rules are somehow technical and complicated. This inevitability requires a special effort to create awareness and reduce the knowledge gaps.

The researcher observed that one of the major challenge of letter of credit operation in Ethiopia is lack of comprehensive awareness of letter of credit both by the bankers and their customers. That actually drags down the quality of banking in letter of credit operations.³⁷⁵ The data collected by Elsa Getnet also shows the same. 66.66 % of the respondents indicated that quality of banking service in the international business transactions are low due to the staff's limited knowledge about the matter and the banks capacity to operate.³⁷⁶ In interview administered by the researcher, all respondents indicated that they do not really know regulatory laws of letter of credit. Specifically, they respond that, they never thought existence of relevant laws that regulate letter of credit in the 1960 Commercial Code of Ethiopia.³⁷⁷

The problem in letter of credit operation is not, however, solely attributable to the banks only. The customers also take a lion share. Majority of customers did not realize the commercial natures of letter of credit and its regulatory frameworks. It is caused by two main factors. One, the literacy level of customers. One researcher revealed that most of customers who use letter of credit are educated at a level of high school.³⁷⁸ Second, the complexity of regulatory rules of letter of credit laws.

In General, limitation towards understanding the law and procedures of letter of credit is caused by, among other things, language barriers. All of the rules and procedures are prepared with English language and they do not have Amharic versions. All of the letter of credit regulatory Directives and Circulars, issued by the NBE, are prepared in English language only. Again, if we look at the banking practice all of the activities relating to letter of credit , such as the application forms, correspondents, letter of credit procedures and the like, are prepared with English language

³⁷⁵ Interview with Sosina Alemayehu, Legal Advisor at Commercial Bank of Ethiopia, on *the awareness of letter of credit regulatory rules and operations in Ethiopia*, 2 April 2018.

³⁷⁶ Elsa, *Assessment on causes of delay in managing International Banking Transaction*, p. 33

³⁷⁷ Interview with Zelalem Asmare, Manager of International Banking Department at Hibret Bank, on *the import and export letter of credit operation in Ethiopia*, 3 April 2018, interview with W/ro Meklit Bekele, Assistant Manager Trade Finance Department at Hibret Bank, on *the practical operation of letter of credit*, 4 April 2018 and interview with W/ro Aster Alemu, Customers Relation Officer of Trade Service at Commercial Bank of Ethiopia, on *the overall letter of credit operation in Ethiopia*, 2 April, 2018

³⁷⁸ Elsa, *Assessment on causes of delay in managing International Banking Transaction*, p. 36

without Amharic versions as counterpart. Predictably, all of letter of credit rules enacted by ICC are in English language and they are not yet translated into Amharic language. When we look the experience of others, many jurisdictions translated UCP600 into their own national languages. That is usually conducted by the ICC national Committees in collaboration with major banks and their associations in the country. To do so, however, there should be prior notification and approval by the ICC, as it has copyright in the documents.³⁷⁹

³⁷⁹ Reinhard, *Documentary credit in Practice*, p. 48

CHAPTER FIVE

CONCLUSION AND RECOMMENDATIONS

5.1. Conclusion

Importers and exporters engaged in international business transactions are often separated by thousands of miles, often take special precautions to ensure performance under their contract. Each party targets to protect its individual interests. The exporter wants to avoid delivering goods for which he might not be paid. The importer, on the other hand, desires the assurance that the seller will not be paid until there is an evidence that the goods have been shipped. There are also other risks such as political and transportation risks in the international trade that the importers and exporters are always anxious about.

To mitigate these risks the commercial community devised an instrument called letter of credit. It is an arrangement by the issuing bank, acting at the request and instruction of the applicant, undertake to pay the beneficiary as long as the latter's presentation complies to the terms and conditions of the credit and relevant laws. It is recognized as one of the ancient commercial instrument that was employed since the time of Ancient Greek and Babylon. The instrument underwent many developments and as of today it is considered as the life blood of international commerce.

In order to utilize its versatile functions letter of credit can be issued in many forms of irrevocable, revocable, conformed, unconfirmed, transferable, back-to-back, differed payment, red-clause, green-clause, acceptance and sight credit.

In Ethiopia, letter of credit operation is recognized as banking business since 1905 with the introduction of modern banking up on establishment of the Abyssinia Bank. However, its application in the import and export transactions was grew in the 1990s following the country's re-introduction of market led economic policy. Currently, due to escalation of import and export transactions, letter of credit operation is amplified in Ethiopia.

Despite the importance of the instrument and its volume of operation in Ethiopia, this research revealed that, the letter of credit regulatory rules in the Commercial Code, and elsewhere, of the country are incomplete, outdated and nebulous.

The first that is revealed in this study is inadequacy of the Ethiopian legal frameworks to regulate vital operations of letter of credit, namely; issuance of letter of credit, amendment of the credit,

revocable and irrevocability of the credit, confirmation of the credit, advising the credit and negotiation of documents. The study has provided a thorough analysis of these operational cycles separately.

It is evident from experience of foreign jurisdictions and also logical that, the laws that deals about issuance of letter of credit are expected to address the issue of formality requirements for establishing letter of credit transactions. However, the relevant sections of the Commercial Code and other regulatory laws are failed to address the issue of formality requirements of letter of credit transactions.

Amendment of letter of credit is also one of the crucial cycle in letter of credit operations. Due to prevalence of errors and problems, amendment of letter of credit is a usual phenomenon that, in fact, happens one in every two letter of credits. However, there is no law in the Commercial Code or elsewhere that can regulates the details of amendment of letter of credit in Ethiopia.

With regard to revocability of letter of credit, the Commercial Code recognized both revocable and irrevocable credit. It further specified the legal effects of both of the credits. Accordingly, revocable letter of credit can be revoked, amended or canceled either by the applicant or the banker at any time without the consent of the beneficiary and the reverse is true for irrevocable credit. At this point whenever the credit or the document establishing is silent as to its status (its status of revocability or irrevocability), the international experiences and banking practice of the country suggests that, presumption of irrevocability should be endorsed. However, the Commercial Code take the reverse one. This makes the code incompatible to the international experience and banking practice of the country.

As far as confirmation of letter of credit is concerned, the Commercial Code consider it as a definite undertaking by the conforming bank, acting at the request and instruction of the applicant, to honor complying presentation of the credit. However, unlike other jurisdictions, the Commercial Code failed to address the issue of silent confirmation. On the other hand, when the credit is unconfirmed, the issue of advising the credit comes in picture. It is one of the major phenomenon in letter of credit operation. It is evident in the study that, the ICC rules, specifically UCP600, and laws of different jurisdictions adequately regulate the subject matter. The Commercial Code, unfortunately, does not have any provision that deals about advising the credit. Nor it has the concept of unconfirmed letter of credit or the so called advising bank.

The last and crucial stage in operation of letter of credit is negotiation of documents. It is comprised of presentation of documents by the beneficiary and payment by the authorized bank provided that the documents tendered by the former strictly conform to the terms and conditions of the credit and relevant laws. Due to its importance, negotiation of documents are given an extensive place in regulatory frameworks of UCP600 and laws of different jurisdictions. The Commercial Code also recognizes presentation of documents and payment as a decisive part of letter of credit operation. The problem in this regard is, the Code failed to specify the documents that are required under letter of credit transactions. Besides, it does not specify general requirements for documents that might be called in the credit. Consequently, banks that operate letter of credit faced challenges of identifying the appropriate documents and their respective requirements (in terms of formality and substance wise). Apart from presentation of documents, it is also failed to properly address the conditions for payment under the credit. Specifically, maturity date of letter of credit and modalities of payments are not properly regulated.

Letter of credit, accompanied by two major governing principles, provides a secured mode of payment in the international trade. The first one is the principle of autonomy. Alike experience of other countries, the principle is enshrined under the Commercial Code. The principle makes letter of credit independent from any other contracts accompanying it. Thus, payment in the credit is confined to the documents presented and not on the goods actually shipped to the importer. This principle no doubt promotes the smooth operation of letter of credit. However, an absolute separation of the credit from the actual performance of the contract creates ample opportunities for fraudsters to abuse the system. They simply forge documents for complying presentation while they ship rubbish or ship nothing at all to the innocent buyer/importer. As indicated in the study, fraud is also committed against banks, exporters and the carries of cargo. In order to tackle the problem, countries pierce the veil of autonomy of letter of credit and develop fraud exception rules. Despite prevalence of the problem in Ethiopia, fraud exception rule is not yet developed.

The second important principle is, the doctrine of strict compliance. It denotes that the documents presented by the beneficiary should be strictly conform to the terms and conditions stipulated under the credit and relevant legal rules. It dictates that, banks should reject any document that is not strictly conform though it can be said almost the same. The Commercial Code of Ethiopia endorsed the principle without any limitation as to its application.

The other prominent aspect scrutinized in this study is parties to the letter of credit and their mutual undertakings in the Ethiopian legal framework. Letters of credit involve a series of complex commercial contractual relations between the applicant, the beneficiary, the issuing bank and the corresponding bank. The study has provided a thorough analysis of the role, as well as, the rights and obligations of all parties involved. It finally revealed that, the Commercial Code has limitation on properly identifying the parties and their respective rights and obligations under the credit.

Due to development of technologies, there is a worldwide move to replace the old document base business dealing by computer, telephone and artificial satellite records. The study ascertained the introduction and increment of electronic letter of credit transactions in Ethiopia. However, electronic letter of credit issues such as electronic signature, retention of electronic records and their evidentiary value in the court of law are matters that badly faced dearth of legal rules in Ethiopia.

Operation of letter of credit, primarily caused by absence of adequate laws, has practically faced several challenges. The primary challenge in this regard is the problem of fraud in transactions. It becomes a threat to letter of credit operation in Ethiopia. The common types of fraud is experienced on documents of bills of lading, insurance policies and commercial invoices. Absence of fraud exception rule hamper proper functioning of the instrument and rights of the innocent party. The other problem is relating to discrepancy of documents. Banks persistently reject documents for very silly errors in the document as a measure of avoiding any responsibility and also to collect fees for each discrepancies. However, when we look from the other edge, it jeopardize the right of the parties as it caused excessive delay, costs and to the worst expiry of the credit.

The other problem in operation of letter of credit is unreasonable time limits set by the banks and NBE. The maximum life span of letter of credit is set for 90 days starting from its issuance date. Besides, NBE sets a maximum of 90 and 120 days for exports (for repatriation of the proceeds) and imports (for clearance of entry of goods in Ethiopia) respectively. These unreasonable time limits cause many letter of credits to expire and some importers and exporters to be in the delinquent list of NBE. Besides, letter of credit operations also challenged because of absence of individual compliant redress mechanisms within or outside the scheme of NBE that can effectively handle letter of credit malpractices. The last, but not least, problem in letter of credit operation is lack of comprehensive awareness about the instrument both by the bankers and their customers.

5.2. Recommendations

In order to solve the aforementioned legal and practical problems accompanying letter of credit operations in Ethiopia, the writer recommends the following.

- ✚ Initially, as formality requirements of letter of credit is not addressed under the Commercial Code or elsewhere, there needs to specify a special formality requirement that takes into account the peculiar characteristics of the instrument. In doing so, the formality requirement should be in the form of records. At this point the record should include both documentary and electronic records. Besides, there should be an authentication requirement
- ✚ In order to resolve problems related to amendment of letter of credit, there should be clear provision in the Commercial Code that regulate the matter. Specifically, the provisions need to address issues such as conditions for amendment of all varieties of letter of credit, the fate of partial acceptance of the amendment, the effect of silence of the beneficiary as to the proposed amendment and the rights of the applicant in amendment of the credit.
- ✚ The presumption of revocability of letter credit (whenever the credit or its establishing document is silent as to its revocability or irrevocability) enshrined under the Commercial Code should be amended and the presumption of irrevocability endorsed so as to cope up with the international experience and Ethiopian banking practices.
- ✚ Regarding confirmation and advising of the credit, the law needs to recognize the full feature of confirmation of letter of credit. To make it specific it needs to recognize the concept of silent confirmation. Besides, the law badly needs to have a rule that can regulate the operation of advising the credit.
- ✚ The laws that regulate negotiation of documents in the Commercial Code needs an intensive revision. In particular it should specify the type, form, number and other requirements for documents required under letter of credit transactions. Besides, the code should incorporate provisions that can regulate maturity date of the credit and the payment modalities.
- ✚ Ethiopia needs to introduce fraud exception rules. The principle of autonomy which is recognized in the Commercial Code does not bother on fraud in the transactions as far as the documents apparently conform to the terms and conditions of the credit. Hence, such loophole should be filled in order to reduce, if not possible to avoid, the enormity of

documentary frauds. The government should not leave such loophole for fraudsters to abuse the system and receive undue benefits as it has a duty to suppress fraudsters in order to keep the business environment healthy and increase credibility of letter of credit in the market.

- ✚ All Commercial Banks need to introduce indemnity agreement schemes to reduce the practical problems caused by discrepancy of documents. Even though strict compliance is the standard for examination and acceptance of documents, it should not be all negligible discrepancies that results failure of compliance and rejection of payments. Accordingly, when the discrepancies are minor and negligible the banks should pay the beneficiary against Indemnity Agreement signed by the parties. It is evident that some of the banks already introduced the scheme, hence, the rest should endorse it.
- ✚ The Commercial Code needs to be revised in order to properly identify the parties in letter of credit transactions. Among other things, the code needs to define all the parties, namely; the applicant, beneficiary, issuing bank, conforming bank and advising bank. Apart from that their rights and obligation should be clearly specified as failure of the code in this regard will make the whole provisions of letter of credit meaningless.
- ✚ Ethiopia needs to introduce electronic letter of credit rules. Documentary credit provisions of the Commercial Code are totally incompetent to regulate electronic letter of credit transactions that are already introduced and that will emerge in the future. Hence, there needs to be a law that can regulate, among others; evidentiary value and retention of electronic records, electronic signature and overall undertakings of the parties in electronic letter of credit transactions.
- ✚ Time limits of letter of credit set by banks and NBE should be revised in order to provide reasonable time for operation of letter of credit transactions. In doing so, the periods should take into account the difference among credits used for different types of imports and exports.
- ✚ The NBE needs to establish an effective individual compliant redress mechanisms in order to redress grievance of customers' against errant banks letter of credit malpractices. As an option, the NBE can introduce Banking Ombudsman Scheme. Thus, the Ombudsman will have the mandate to receive individual complaints and resolve the problem either by consultation, award the injured party or penalizing the perpetrator bank.

- ✦ Finally, in order to avoid problems of letter of credit operations caused due to lack of awareness, there should be awareness creation for bankers and their respective customers.

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9. Interview with W/rit Almaz Mengstu, Customers Relation Officer at Wegagen Bank, *on the overall letter of credit operation in Ethiopia*, 4 April 2018
10. Interview with Ato Melaku Mekonen, Manager of Legal Service Division at Ethiopian Shipping and Logistic Service Enterprise, *on the issue of Fraud relating to bill of lading in letter of credit transactions*, 4 April 2018
11. Interview with Adugna Amaha, Foreign Exchange Inspector at National Bank of Ethiopia, *on the malpractices relating to letter of credit operations in Ethiopia*, 3 April 2018
12. Interview with Mesfin Getachew, Chief Legal Expert at National Bank of Ethiopia, *on historical background of letter of credit in Ethiopia*, 6 March, 2018
13. Interview with Ato Anteneh Girma, Manager of Credit Service Central Processing Unit at Commercial Bank of Ethiopia, *on letter of credit operation in the Ethiopian Banking Practice*, 5 March 2018
14. Interview with Sosina Alemayehu, Legal Advisor at Commercial Bank of Ethiopia, *on the awareness of letter of credit regulatory rules and operations in Ethiopia*, 2 April 2018

List of Attachments

Attachment 1: Letter of Credit Application Form

Application for Letter of Credit

To: CBE _____ Branch _____ Date _____

Applicant's Name and Address _____

License No. _____ Type (Trade/Industry/Investment) and TIN No. _____

Please indicate your choice with "x" mark in the box

Source of Fund: Reserve Grant Foreign Loan, loan number: _____

NRE Account Number for FCY request: _____

Beneficiary's (Supplier's) Name and Address: Supplier

Name and Address of Advising Bank: _____

(If especially needed) _____

1. L/C Type Confirmed Transferable

2. Available By: Payment Negotiation Acceptance Deferred Payment Mixed Payment

3. Amount in figures: (FCY) _____, Amount in words _____

4. Delivery Term: _____

5. Shipment Date : Not later than _____

6. Expiry Date: Not later than _____

7. Shipment form _____ 8. Shipment to _____

9. Partial shipment: Allowed Not Allowed 10. Transshipment: Allowed Not Allowed

11. Shipment to be effected by: Ethiopian Shipping Lines Ethiopian Air Lines Other

12. Country of Origin of Goods _____

13. Package to be Marked _____

14. Charges of all Banks outside Ethiopia are for account of: Applicant Beneficiary, if there is any other

Condition _____

Documents Required

× 15. Bill of Exchange/Draft: Required Not Required 16. Freight Invoice: Required Not Required

✓ 17. Signed Commercial Invoice: Specifying freight and insurance when the delivery term indicated involves them, and originals should be certified by Chamber of Commerce. Number of originals Number of copies

18. Signed Manufacturer Invoice: Number of originals Number of Copies Certified by Chamber of Commerce or not.

✓ 19. Packing Lists: Number of originals Number of Copies

✓ 20. Transport Document marked Freight Payable at destination Prepaid by the shipping Company.

Full set of Clean on Board Ocean Bill of Lading Truck Way Bill/Receipt Other _____

Original Airway Bill Parcel Post Receipt

Railway Receipt Courier bill

Made out to the order of _____ Marked Notify _____

LC - 1001

Attachment 2: Letter of Credit Sample

COMMERCIAL BANK OF ETHIOPIA
TRADE SERVICE CENTRAL PROCESSING CENTRE

LETTER OF CREDIT

Date : 19/05/08

TO ETHIOPIAN GRAIN TRADE ENTERPRISE
P.O. BOX 3321
TELL 0114653166
ADDIS ABABA, ETHIOPIA

WE HAVE RECEIVED IRREVOCABLE LETTER OF CREDIT UNDER OUR REFERENCE
NUMBER
2008.EL.00000131

Issuing bank ABN AMRO BANK (PAKISTAN) LIMITED
ICPU TRADE OPERATION, KARACHI
KARACHI, PAKISTAN

:27:SEQUENCE OF TOTAL
1/1
:40A:FORM OF DOCUMENTARY CREDIT
IRREVOCABLE
:70:DOCUMENTARY CREDIT NUMBER
NLNLINL08B104142
:31C:DATE OF ISSUE
080519
:40E:APPLICABLE RULES
UCP LATEST VERSION
:31D:DATE AND PLACE OF EXPIRY
080721 IN BENEFICIARY'S COUNTRY
:50:APPLICANT
PATEL AND CO.
207 GRAIN CENTER, DANDIA BAZAR,
KARACHI, PAKISTAN.
:59:BENEFICIARY
ETHIOPIAN GRAIN TRADE
ENTERPRISE
P.O. BOX 3321
TELL 0114653166
ADDIS ABABA, ETHIOPIA
:32B:CURRENCY CODE, AMOUNT
USD350000.00
:39B:MAXIMUM CREDIT AMOUNT
NOT EXCEEDING
:41D:AVAILABLE WITH...BY...
ANY BANK IN ETHIOPIA
BY NEGOTIATION
:42C:DRAFTS AT...
SIGHT
:42D:DRAWEE
FORMERLY PRIME COMMERCIAL BANK
LTD,

//



ኢትዮጵያ ፌዴራላዊ ዲሞክራሲያዊ ጥቅም አዲሲያ ባንክ ሲ.ቤ.ቤ

የኮ/መ/ቁ 134400

ቀን 18/10/2006 ዓ.ም

ዳኛ - ብርሃኑ መንግስቱ

ከሣሽ - የኢትዮጵያ ይህል ገንድ ድርጅት ነ/ፈ.ጅ ጌታሁን ደምዕስ ቀረቡ

ተከሣሽ - የኢትዮጵያ ገንድ ባንክ ጠመንጃ ያዥ ቅርንጫፍ ነ/ፈ.ጅ ሶስና ገበየሁ ቀረቡ

መዝገቡ ተመርምሮ ከዚህ የሚከተለው ፍርድ ተሰጥቷል።

ፍርድ

ጉዳዩ አለም አቀፍ ሽያጭን መሠረት በማድረግ በባንኩ የሚሰጥ የብድር /መተማመን/ ሰነድ ወይም Letter of credit የሚመለከት ሲሆን ከሣሽ ግንቦት 26 ቀን 2005 ዓ.ም ሰር ያቀረበው ክስ ይዘት ከዚህ የሚከተለው ነው።

ከሣሽ ፖቴልና ከባንያው ወይም የሚኒ ግሬን ሴንተር ጸንዲያ፣ ባዛር፣ ጋራ፣ ለተባለው ተተማጭነት ጸንዲያ ባዛር ፖሊስታን ከሆነው ድርጅት ጋር በውል ቁጥር CD15705 ሚያዝያ 24 ቀን 2000 ዓ.ም ተ 400 ሚ/ቱን ሽንብራ ሽያጭ ውል አድርገዋል። የሽንብራ ሽያጭ ውል በሚ/ቱን ዋጋ 700.00 የአሜሪካን ዶላር ሲሆን የ 400 ሚ/ቱን ዋጋ 280,000.00 የአሜሪካን ዶላር በመሆኑ በኢትዮጵያ በወቅቱ በነበረው ምንዛሪ ብር 2,699,396.00 የሆነውን ክፍያ በምንጠባበቅበት ጊዜ ገዥው የተለያዩ ምክንያቶችን በመፍጠር ክፍያው ሳይፈጸም ጋልን ቀርቷል።

በመሠረቱ ገዢው በአገሩ ባንክ አል ሲ የክፈተ ሲሆን ባንኩ ደግሞ በሻጭ አገር አልሲ ክፍቷል። የዱቤ ገዢው ባንክ ገዢውን ከባንያ የሚጠራጠረው ሲሆን እንኳን ገዢው እንዲከፈትለት ለሚጠይቀው አካል ሲገዢው ውሉን ባይፈጸም ግዴታውን ለመወጣት የሚያስችለው የገንዘብ መጠን እንዲያስይዝ ማድረግ አለበት። በአልሲ የባንክ አሠራር ሥርዓት መሠረት ገዢው ምርቱን ከወሰደ በኋላ ገንዘቡን ባይከፍልበት ብሎ የማይሰጠው ሁኔታ የመምርቱን መጫን ለክፍያ መፈጸሙ ወሳኝ ቅድመ ሁኔታ ሲሆን ሽጩም ሲሆን ምርቱን ከላክ በኋላ ገዢው ክፍያውን አልፈጸምም ቢልበት ብሎ የማይፈጸም ምክንያት የአል ሲው መክፈት

[Handwritten signature]



Scanned by CamScanner

የፍ/ይ/መ/ቁጥር--104049
ቀን-ሐዳር 22 ቀን 2008 ዓ.ም

ጻፍኛ:- ገበየሁ ፈለቀ

በዕውቀት በላይ

አለማየሁ ሹናራ

ይግባኝ ባይ:- የኢትዮጵያ እህል ንግድ ድርጅት ነ/ፈ.ጅ-ይግራም ነጋሽ ተረቡ

መልስ ሰጪ:- የኢትዮጵያ ንግድ ባንክ ነ/ፈ.ጅ ወ/ር አያንቱ ባጫ ተረቡ

መዝገቡ የተተጠረጠ ለምርመራ ሲሆን፤ የሚከተለው ፍርድ ተሰጥቷል።

ፍርድ

ይግባኝ የተረጠጠ የፈ.ጅ.ል ከፍተኛ ፍርድ ቤት በክ/መ/ቁ 134400 ሰኔ 18 ቀን 2006 ዓ.ም በሰጠው ወላኔ ቅር በመሰኘት ይግባኝ ባይ ነሐሴ 12 ቀን 2006 ዓ.ም የተጻፈ የይግባኝ አቤቱታ በማቅረቡ ነጩ። የአሁኑ ይግባኝ ባይ በስር ፍርድ ቤት ከላሽ ሲሆን መልስ ሰጪ ደግሞ ተከላሽ ነበረ።

በስር ፍርድ ቤት ይ/ባይ አቅርቦት የነበረው ክስ ይዘት በአጭሩ:- ይ/ባይ ፓቲልና ኩባንያ ዌም ሮሜኒ ግራን ሰንተር ጽንጻያ፣ ባዛር ጋራ፣ ለተባለው ተቀማጭነቱ ጽንጻያ ባዛር ፓኪስታን ከሆነው ድርጅት ጋር በወል ቁጥር CD15705 ሚያዝያ 24 ቀን 2000 ዓ.ም የ400 ሚፊትን ሽምብራ ሽያጭ ወል እድርገናል። የሽምብራ ሽያጭ ወል በሚፊትን ዋጋ 700 የአሜሪካን ዶላር ሲሆን ሆኑ የአጠቃላይ ዋጋ 280,000 የአሜሪካን ዶላር ወይም በወቅቱ በነበረው ምንዛሪ ብር 2,699,396 የሆነውን ከፍያ የተለያዩ ምክንያት በመፍጠር ሳይፈጽምልን ተርጉሟል። ሽያጭ በአገሩ ባንክ አል ሲ የክፈተ ሲሆን ባንኩ ደግሞ በሻጭ አገል አል ሲ በተከላሽ ባንክ ከፍቷል።

ይ/ባይ በወሎ መሠረት የሽምብራ ምርቱ ድቡቲ ወደ-በ የደረሰበትን ሰነዶች በሙሉ በተከላሽ በኩል ለኮርሰፖንደንት ባንኩ አዲ አን አለም አርት ባንክ ፓኪስታን መሳካቸውና ደርሰው ተቀባይነት ይገኝ መሆናቸውን ተከላሹ አረጋግጧል። በወሎ መሠረት የከሰደትና ጥራት ደረጃ ቁጥጥር መደረግ ያለበት ምርቱ በሚሟገበት ጊዜ መሆኑ በግልጽ ተቀምጧል። ነገር ግን ከወላችን ወጭ ሽያጭ ኩባንያ በተረከበው ምርት ወሰጥ ነፍሳት አግኝቻለሁ ሲል ያነሳውን ተቀባይነት የሌለው ሀሳብ ባቻ በመቀበል ተከላሹ ኮርሰፖንደንት ባንኩን የምርቱን ዋጋ ማስከፈል ሲገባው የማጻጻግ ሰነዶችን የሻጭ አማካሪ የነበረው ተከላሽ ባይ ምክንያት ከአሁን ወጭ ነጩ። በመሆኑም ከገዥ ለሚፈለገው ዕዳ በንግድ ሕግ አንቀጽ 963 መሠረት

የፍርድ ቤት ማህተም
ሐዳር 22 ቀን 2008 ዓ.ም
የፍርድ ቤት ማህተም
963 መሠረት

149

Attachment 5: Grain Trade Enterprise v. Commercial Bank of Ethiopia, Federal Supreme Court Cassation Division, 2010, Civil Case No.123162



የሰ/መ/ቁ 123162

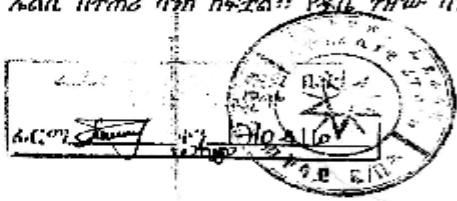
ቀን 09/04/2010 ዓ.ም

ዳኛቸ :- ተሸላኝ ይመልሰል
 ተረፎ ገለግሎት
 ቀን 9 ቀን
 ተሸላኝ ሸራራው
 ፀሐይ መንከር

አመልካች :- የኢትዮጵያ የሌላ ገንዘብ ድርጅት የቀረበ የሰነድ
 ተጠሪ:- የኢትዮጵያ ገንዘብ ባንክ ነገረ ፈጅ የከተለ ስለሽ ቀረበ
 መዝገብ ለምርመራ ያደረ ሲሆን መዝገብ መርምረን ተከታይን ፍርድ በጥተናል ::

ፍርድ

1. በዚህ መዝገብ ለከፊላዊ የሆነውን መሠረታዊ ሂሳብ ለማግኘት ወል መነሻ ባደረገው አድራሻ/letter of credit / የሌላ ተጠሪ ከአመልካች ጋር ባደረገው ውል መሰረት የነበረው ሚና እና የተጠያቂነት እድገት አስከፊ ምን ድርሰ ነው? የሚል ነው:: በሥራ በተደረገው ክርክር አመልካች ከሰነድ ተጠሪ ተከላኝ ነበሩ:: አመልካች ገንዘብ በየደረጃው የተመለከተን ፍርድ ሲቀጥ የሰነድ ፍርድ መሠረታዊ የሆነ ስህተት የተፈጸመበት በመሆኑ በዚህ ጉዳይ ሊታረም ይገባል በማለት ያቀረበው አቤታታ አጣርቶ ለመወሰን የቀረበ ነው::
2. በሰር ፍርድ ቤት አመልካች ያቀረበው ከሰ ጥያቄ:- አመልካች ፓቴልና ኩባንያ ዌም ሮሚኒ ግሪን ሲገተር ዳገዲያ ባህር ጋራ ለተባለው ተቀማጭና ተዳጋይ ባህር ፓኪስታን ከሆነው ድርጅት ጋር በውል ቁጥር CD15705 ሚያዝያ 24 ቀን 2000 ዓ/ም የ400 ሜትር ሜትሪክቶን ሸንብራ ውል ሸያዎ ውል ለደርገናል:: የሸንብራ ሸያዎ ውል በሜትርክ ቶን ዋጋ 700 የላሜሪካን ዶላር ሲሆን የአጠቃላይ ዋጋ 280,000 የላሜሪካን ዶላር ወይም በወቅቱ በነበረው ምንጭ ብር 2,699,396 የሆነውን ክፍያ የተለያዩ ምክንያት በመፍጠር ሳይፈጸምልን ቀርቷል:: ሽግግር በሌላ ባንክ አልሲ የከፈተ ሲሆን ባንኩ ደግሞ በሽግግር አገር አልሲ በተጠሪ ባንክ ከፍቷል:: የደብ ሽግግር ባንክ



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