

Documentary Letters of Credit in Iraqi Law

Introduction;

The assay demonstrates the system of payments of international goods by the means of letter of credit, The study shows the types of LC in Iraqi commercial legal system_by the influence of international chamber of commerce rules ICC ,in addition to Iraqi judicial decisions relates with.

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Bank credit either takes the form of a monetary sum provided by the bank to a client as a loan, or the form of a guarantee the bank provides to a client. This guarantee allows the client to obtain the confidence of other parties, who will then grant the client a delay [in payment], or enter into a contract with him, reassured that their rights are guaranteed by the bank's involvement. When providing this type of credit, the bank does not extend immediate funds.

Letters of credit are one of the most important and widespread forms of bank credit in the field of foreign trade. In particular, they are used to finance maritime trade, because they employ commercial banks as intermediaries, due to the considerable financial capabilities of these banks, and to their reputation among exporters and importers.

Financing of foreign trade and international exchanges takes the following forms:

1- Direct Monetary Financing.

Under direct monetary financing, the importer sends the value of the goods to the exporter who ships the goods upon receipt of the amount, whether in cash, wire transfer or check.

2 – Payment after the goods are shipped and have reached the buyer.

3 – Drawing a bill of exchange on the buyer that is sent along with the shipping documents, which are not handed over to the buyer until the amount on the bill of exchange has been paid, or the bill is accepted.

4 – Documentary letters of credit for maritime trade.

5 – Documentary letters of credit take many forms as follows:⁽¹⁾

I. According to the bank's obligation towards the beneficiary, documentary letters of credit may either be revocable or irrevocable.

II. Documentary letters of credit may be either general or special. A general letter of credit is not addressed to a specific bank, and

any bank may serve as the intermediary; whereas a special letter of credit is addressed to a particular bank.

III. Import and Export Letters Of Credit

Letters of credit are used to settle import and export transactions in international trade. When a letter of credit is drafted to conclude an export transaction, it is called an export letter of credit. Similarly, when a letter of credit is drafted to conclude an import transaction, it is called an import letter of credit.

Importing and exporting is a two-sided operation, which is considered as importing from the buyer's standpoint and as exporting from the seller's.

Letters of credit of this type may require certain measures in some countries such obtaining an authorization, particularly by the importer and exporter, which gives guarantees to the competent authorities. The authorities then ensure that the values of exported goods will be remitted [to the exporter]. In Iraq, authorizations are granted under Law No. 19 of 1961 Overseeing the Transfer of Funds Abroad, as amended.

IV. Local or Domestic Letters of Credit and Foreign Letters of Credit

Letters of credit are local if a bank in the same country intermediates to settle the transaction, and are foreign if correspondent banks intermediate from abroad.

V. Transferable and Non-Transferable Letters of Credit

A letter of credit is transferrable if it allows the beneficiary to transfer all or part of the credit value to another beneficiary.

VI. Divisible Letters of Credit

This type allows the shipment of goods in several batches rather than in one shipment.

VII. Sight Letters of Credit, Anticipatory Letters of Credit, and Deferred Payment Letters of Credit

Sight letters of credit are payable upon sight of documents. If payment is required to be made in advance, the letter of credit is called an anticipatory letter of credit. This type may allow [the seller] to draw up to a specific amount (10% for example) of the amount on letter of credit, before the bills of lading are presented. These terms are written in red ink (red clause letter of credit). Iraqi banks open letters of credit with advanced payment without the red clause. Payment is made in advance against a receipt or a pledge from the buyer to ship the goods. There is also what is known as “green ink clause” credit.

VIII. Revolving or Renewable Letters of Credit

Transaction circumstances may require the issuance of a letter of credit with certain drawing limits renewable on a regular basis for the purpose of funding the import of goods. The amount of this type of letter of credit is renewed automatically under the same terms throughout a number of cycles. After each cycle is completed, the value of the letter of credit is renewed in full for the next cycle.

IX. Secured and Unsecured Letters of Credit

If the shipping documents are issued in the name of the buyer, to the buyer’s order, or the seller’s order, and are endorsed to the buyer, the bank does not have power over the goods and hence the letter of credit is unsecured.

X. Back-to-Back Letters of Credit

The original beneficiary, upon receipt of a notification that a letter of credit has been opened in his favor by the buyer, opens another letter of credit (ancillary letter of credit), with the letter of credit opened in his favor as collateral.

These are the types of letters of credit recognized by the Iraqi legal system.

The Use of Letters of Credit (Court Decisions)

Before presenting the rulings of Iraqi courts, it is crucial to note that Iraq witnessed a period characterized by state control of all internal and external trade services, due in particular to a centralized system based on the theory of planned economy. This was especially the case after the Iraq-Iran war in 1980, the Iraqi occupation of Kuwait in 1990, the promulgation of numerous international resolutions against Iraq, and the imposition of the Memorandum of Understanding pertaining to “Oil for Food and Medicine” during the economic embargo following the Kuwait war. These factors had a negative effect on foreign trade; therefore, the majority of judicial rulings date to the period prior to 1980.

After 1990, the State banned the transfer of funds abroad. Articles 92-161 of the Commercial Law No. 30 of 1984 authorized payment in foreign currency, but such payment was banned by a decision issued by the now-dissolved Revolutionary Command Council (RCC). In 1990, the RCC issued decision No. 98 of 1999 [sic] permitting the transfer of funds abroad. Nevertheless, a number of cases involving documentary letters of credit are outlined below.

I. Case No. 222/72 dated March 26, 1972; dossier 9846 (Court of Cassation)⁽²⁾.

A Jordanian supplier presented to an Iraqi bank bills of lading pertaining to a shipment of tomatoes, but when the Iraqi importer visited the customs department to clear the goods, he discovered that the Jordanian supplier had not shipped the goods. The supplier had acted in collusion with the carrier to obtain a bill of lading. Thus, the fraud and collusion were perpetrated by the exporter. It is easier to obtain a bill of lading with forwarding fees when the submission of a standard bill of lading is required. A bill of lading with forwarding fees is a receipt by means of which a carrier acknowledges receipt of the goods described

therein and pledges to transport said goods on board a named or unnamed vessel to their destination and also to deliver the shipment to its rightful consignee. A “bill of lading with forwarding fees” is a promise to ship goods and does not signify that the goods have actually been shipped.

II. Court of Cassation Decision 627/H/1968 dated November 28, 1968⁽³⁾

Decision: (According to the interpreters’ interpretation of Article 12 of the Uniform Customs and Practice, if the issuing bank that opens the letter of credit seeks the assistance of another bank to execute the letter of credit, the issuing bank is responsible for its mistakes and those of the bank it used.

However, if the issuing bank is only an agent in contracting another bank to open or support a letter of credit, the issuing bank is responsible for the mistakes of the correspondent bank that it used to examine the documents, should the issuing bank be blamed for negligence in monitoring the correspondent bank).

Note: In 1968, Iraq did not have a law to regulate letters of credit. The Commercial Law No. 60 of 1943 was the applicable law at the time and did not provide for letters of credit. Hence, the [court’s] decision cited the Uniform Customs and Practice. Regulation of letters of credit⁽⁴⁾ appeared for the first time in Commercial Law No. 149 of 1970, which was repealed and replaced by Commercial Law No. 30 of 1984, which remains in effect at the present time. As mentioned above, Articles 273-282 of this law regulate letters of credit.

Decision (continued):

(Whereas it was the defendant who had opened the letter of credit and had used the correspondent bank to do so; and whereas by opening the letter of credit the bank becomes liable if the terms of the letter of credit are breached or if the accuracy of the documents is not confirmed, then the defendant is deemed to have violated the terms of opening the letter of credit because the defendant did not verify the weight).

III. Court of Cassation Decision dossier No. 200 /H/ 965 dated February 26, 1966⁽⁵⁾

Decision: (After the seller fulfills his obligation to submit documents, and these documents are then deemed by the bank to conform to the terms according to which the letter of credit was opened, the bank has no right of recourse against the seller on the grounds that it has discovered that the goods had become damaged during transport due to an unforeseen cause).

IV. Decision of the Baghdad Court of Appeals, Decision 216/248/appeals/1969, dated March 5, 1970,⁽⁶⁾ The Court of Cassation upheld this decision stating that (In this case, the responsibility of the bank ends when it establishes the conformity of these documents to the document used in opening the letter of credit).

V. Decision of the Iraqi Court of Cassation, 41/general panel/1971, dated June 26, 1971⁽⁷⁾

Decision: (In their dealings with their clients at home and abroad, the public interest is served when banks are considerate of their clients' interests and are as attentive to their clients' funds as they are to their own profits. Should such attentiveness be lacking in the banks' implementation of their obligations, they are to be held accountable to those who do business with them).

VI. Decision of the Baghdad Court of Appeals, Q/159/64 dated November 14, 1964; dossier at the Court of Cassation 391/H/965 dated June 27, 1966⁽⁸⁾.

Decision: (The terms of opening a letter of credit waive the liability of the bank regarding the validity of the documents and the description of the goods as well as their type and value).

VII. Court of Cassation Decision No. 200/H/965 dated February 26, 1966,⁽⁹⁾

Decision: (The seller fulfilled his obligations by submitting documents that the bank found to be in conformity to the terms of opening the letter of credit. If the bank did not adequately determine the conformity of the documents or if it accepted the

non-conforming documents, the bank bears the burden of its error).

VIII. Decision No. 627/H/68 dated November 28, 1968⁽¹⁰⁾

Decision: (When a bank accepts documents that do not comply with the terms of the letter of credit based on a pledge by the seller to repay the bank the amount it paid to him if the buyer does not accept these documents, i.e. disbursing payment to the buyer with reservations, the buyer's right to reject these documents is not affected. The bank cannot **oblige the buyer to accept the documents on the grounds that the payment disbursed with reservations preserves the buyer's right to challenge the seller** because the pledge obtained by the bank from the seller in return for accepting documents that do not conform to the terms of the letter of credit is intended to protect the bank and not the seller in the event the buyer refuses to accept the documents.

IX. Decision of the Court of Cassation, 41/general panel/Cassation dated June 26, 1971,⁽¹¹⁾

Decision: (The bank is liable for the shortage in the amount of coal because it neglected to inspect the bill of lading to verify the weight of the shipment, and it failed to confirm compliance with the terms of the letter of credit).

X. Decision on partial shipment (letter of credit based on shipping in batches) Court of Cassation Decision 391/H/965 dated June 27, 1966⁽¹²⁾.

Facts of the case: An irrevocable letter of credit was opened by Company (T) at the Arab Bank in Baghdad on January 12, 1960 in the amount of 6,500 pounds to import 500 radiophones. The letter of credit, which was to remain effective until February 23, 1961, indicated that the radiophones were to be sent in four shipments, but it did not specify a shipment date. Therefore, Article 34 of the Uniform Customs and Practice does not apply. The first shipment was received on December 31, 1960 (288 radiophones with their accessories with a value of 3,744 pounds). Then a second shipment was received: (211 radiophones with their accessories and with a value of 2,756 pounds). The

Company objected to this shipment on the grounds that it did not conform to the terms of the letter of credit which dictated that the goods be shipped in four batches. The Arab Bank was informed of this rejection by means of a written notice. The documents were returned and the payment was considered void.

Then the supplier furnished bills of lading for a third shipment of 181 radiophones with a value of 2,457 pounds. These bills of lading indicated that the balance of the letter of credit amount, 296 pounds,

would be used by the supplier to ship two batches from Hamburg before the expiration of the letter of credit on February 23, 1961. The Company refused the documents on the grounds that they did not conform to the terms of the letter of credit. The case that was filed by the Company was dismissed by the Court of First Instance, the Court of Appeals and the Court of Cassation. The Company then requested that the letter of credit be amended. This request was rejected because the terms of the letter of credit did not provide for equal shipments, because the letter of credit was irrevocable and because the Arab Bank did not violate the terms of the letter of credit when it paid the beneficiary.

Note: The decision falls within the jurisdiction of the Commercial Law No. 60 of 1943, which lacks provisions to regulate letters of credit; therefore, the Uniform [Code of] Customs and Practice was cited.

XI. A case presented before the judicial committee entrusted with monitoring foreign exchange transactions by the Central Bank pursuant to the Law No. 91 of 1961 on the Transfer of Funds Abroad, as amended.

Summary of the case: An Iraqi bank and an Iraqi importer were sued and accused of violating the requirements of the Foreign Exchange Law by transferring funds abroad to pay for imported goods that were never delivered to Iraq. Briefly, an Iraqi merchant had agreed with a foreign supplier to import quantities of lumber from said supplier, who would be paid for the imported lumber through letters of credit opened in favor of the foreign

supplier. A sum that is 25% of the value of the lumber was to be paid in advance, and the balance was to be paid in future drafts. The Iraqi bank accepted the documents as conforming to the terms of the open letters of credit. Afterwards, it became clear that the documents were fraudulent and did not represent goods shipped in implementation of the letters of credit. It also became evident that the supplier was an impostor who had defrauded the Iraqi merchant. The bank was not considered liable for accepting the documents on the grounds that it was not the bank's duty to verify the validity of said documents. The judicial committee decided the following:

(The bank is not considered to have erred in the implementation of its obligation to examine the documents and disburse payments to the beneficiary on the basis of these documents, if they appear to be authentic, even if they are later found to be fraudulent. The bank is not liable for that, and the buyer bears responsibility for the damages that resulted from the poor choice he made in selecting a business partner).

XII. Decision of the Court of Cassation, 627/H/68 dated November 28, 1968,⁽¹³⁾

The decision is an interpretation of Article (12) of the Uniform [Code of] Customs and Practice.

Decision: (If the issuing bank seeks the assistance of another bank, the issuing bank becomes liable for its mistakes and for those made by the bank whose assistance it had sought.

However, if the issuing bank is only an agent in contracting with another bank to open or support a letter of credit, the issuing bank alone is liable for its mistakes as well as those of the correspondent bank whose assistance it had sought to examine the documents, should the issuing bank be blamed for negligence in monitoring the correspondent bank).

XIII. Decision No. 200/H/1965 dated February 26, 1966,⁽¹⁴⁾

Summary of the case: An Iraqi national entered into a contract to export dates (Zuhdi Al-Furat). Letters of credit were opened at Banco Espanol in Tetouan in favor of an Iraqi seller, with the Arab Bank acting as intermediary. The Iraqi exporter submitted

documents to the Arab Bank, and the Arab Bank accepted them and disbursed funds to him. When the Arab Bank sent the documents to the issuing bank (Banco Espanol in Tetouan), the latter refused to issue payment to the Arab Bank on the grounds that, on the one hand, the documents did not conform to the letters of credit and, on the other hand, the quality of the dates was poor. The Arab Bank filed a lawsuit against the Iraqi merchant demanding payment of the amount it had paid. The Court of Cassation ruled that the Arab Bank was not entitled to seek payment from the seller because the letter of credit was irrevocable. The bank should have refused [to accept the documents] when it found them to be non-conforming to the terms of the letter of credit. And yet, when the bank discovered the violation, it did not inform the beneficiary of this violation or deficiency through the intermediary bank.

Decision: (The bank is not entitled to refuse payment of funds drawn under the letter of credit and at the request of the buyer regardless of the reasons invoked by the buyer in the context of his relationship with the seller. The bank was considered responsible for withholding payment from the buyer).

XIV. An advisory opinion issued by the State Consultative Council on April 3, 1990,⁽¹⁵⁾

The electrical industries facility asked the Central Bank to withhold payment of an amount from letter of credit No. ----- - and to withhold payment of another amount from letter of credit No. ----- . The facility claimed that the bills of lading for shipments had been submitted, but that the goods had not arrived, or they had arrived but were not in compliance with technical specifications, or that the shipment was incomplete. A legal opinion was requested regarding the request made by the facility to the Central Bank to withhold payment of the specified two amounts from the specified two letters of credit. Central Bank Advisor Khaled Shaker issued an opinion, and the decision to withhold the amounts was upheld.

Conclusion:

From the study it's obvious that one of the means of paying the values of international goods is the system of letter of credit.

This system is developed progressively in Iraq due to the modern rules applied which confirm it from the custom rules of ICC in order to attract foreign investors to rebuild Iraqi infrastructures.

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الاعتمادات المستندية في القانون العراقي

البحث يمثل دراسة وجيزة عن الاعتمادات المستندية في القانون العراقي من حيث بيان مفهومها الوارد في قانون التجارة النافذ رقم 30 1984 , وانواعها ومدى تطبيقها في العراق طبقاً لما ورد في نشرة الاعراف للاعتمادات المستندية (UCP600) التمييز القديمة والحديثة للتعرف على التطبيقات القضائية التي تؤكد على وجود الفصل بين العقد الرئيسي وعقد الاعتماد و الاستناد الى النشرة الموحدة للاعتمادات المستندية في حالة عدم وجود ن .