

**IN THE SUPREME COURT OF THE DEMOCRATIC SOCIALIST**  
**REPUBLIC OF SRI LANKA**

In the matter of an appeal in terms of Chapter LVIII and in particular in terms of Section 754 (1) of the Civil Procedure Code read together with the provisions of Sections 5 and 6 of the High Court of the Provinces (Special Provisions) Act No. 10 of 1996 against the Judgment of the learned High Court Judge of the Commercial High Court of Colombo delivered on 10.06.2004.

**SC. CHC. No. 41/2004**

HC. Civil Case No. 255/2002(1)

People's Bank,  
No: 75, Sir Chittampalam A. Gardiner  
Mawatha,  
Colombo 2.

**Plaintiff-Appellant**

-Vs.-

Good Fellows (Pvt) Ltd.,  
No. 50/22, Mayura Place,  
Colombo 5.

**Defendant-Respondent**

**BEFORE** : **Tilakawardane, J.**  
**Ekanayake, J. &**  
**Dep, PC, J.**

**COUNSEL** : Kushan D Alwis, PC, with Kaushalya Nawaratne  
and Hiran Jayasuriya for the Plaintiff-Appellant.

M.U.M. Ali Sabry, PC, with Sanjeewa Dassanayake  
for the Defendant-Respondent.

**ARGUED ON** : 08.07.2013

**DECIDED ON** : 30.07.2013

**Tilakawardane, J.**

The Plaintiff – Appellant (hereinafter referred to as the Appellant Bank) instituted action against the Defendant – Respondent (hereinafter referred to as the Respondent) in the Commercial High Court of the Western province holden in Colombo in case No. 255/2002 seeking to recover a sum of US \$ 347,972.72 and a sum of US \$ 288,163.16 based on two Letters of Credit (marked as ‘P3’ and ‘P6’).

The Learned Judge of the Commercial High Court dismissed the Appellant Banks case by its judgment dated 10.06.2004. The Appellant Bank has now filed this appeal against the said judgment of the Commercial High

Court, on the following questions of Law.

1. The Learned Judge of the Commercial High Court had erred in law in holding that in the case of non-payment of the monies granted to the Respondent, the Appellant Bank can have a right to recover the said monies only on the issuing bank.

The Learned Judge of the Commercial High Court had misunderstood the action of the Appellant Bank to be an action instituted under the terms of the Letter of credit when in fact the action is based on the Guarantees marked as 'P10' and 'P11'.

A Company under the name of 'Speed Control New York Inc.' agreed to purchase certain goods from the Respondent. The payment for the said sale was organized through irrevocable Letters of Credit. In Terms of the said Letters of Credit 'Speed Control New York Inc.' which is the buyer, requested the 'Marine Midland Bank New York', the issuing bank, to open a documentary credit in favor of the Respondent, the Seller and/or Beneficiary. The Appellant Bank negotiated several Bills drawn under the said Letter of Credit and monies were paid to the Respondent (marked 'P3' and 'P4'). The Respondent has executed several guarantees to the repayment of the said monies. However, the Appellant Bank claims that no monies have yet been paid to the Appellant Bank.

The Appellant Banks case is that the Respondent has failed and neglected to pay the sums due to the Appellant Bank; however, the Respondent denies the Appellant Banks claim, on the basis that any liability to make payment under the Letters of Credit lies only with the issuing bank.

The Respondent's position is that, the issue has arisen in consequence of

negotiating a letter of credit bearing No. DC MTN 953706 originally for a sum of US \$ 1,247,870/- issued by the Marine Midland Bank of New York in favor of the Respondent. The Respondent negotiated the said Letter of Credit with the Appellant Bank and assigned its rights under the said Letter of Credit in favor of the Appellant Bank in lieu of the funds received by the Respondent. Once the Letter of Credit has been given in favor of the Appellant Bank and the Respondent had exported the goods and handed over all relevant documents to the Appellant Bank, it is the responsibility Appellant Banks to seek payments from the said Marine Midland Bank of New York (Issuing Bank) based on the said Letter of Credit. Since the said Letter of credit was a clean bill, the Appellant is best able to recover the monies from the said issuing Bank.

The counsel for the Respondent further asserted that once the Appellant Bank had already referred the dispute for arbitration in the International Chamber of Commerce, that the Appellant Bank cannot redress remedies against the Respondent until the final determination from the International Chamber of Commerce is delivered.

The internationally accepted documentation for imports and exports, the Documentary Credits/ Letters of Credit are governed under the Documentary Credit and the Uniform Customs and Practices. The Uniform Customs Practices are binding on banks, the applicants for the credits and their beneficiaries. [*Goldets V Czarnikow (1979) All ER 726*]. Accordingly, where a contract for the sale of goods provides for payment to be made by a bankers letter of credit, it is the buyers duty to arrange with the bankers for a documentary credit to be issued in favor of the seller in the currency specified.

## **SC. CHC. No. 41/2004**

A documentary credit issued by a creditworthy bank, guarantees payment to the seller on condition that he presents the correct documents and does so independently of the underlying contract of sale. The issuing bank's creditworthiness is substituted for that of the buyers, and this security for the seller is normally the fundamental purpose of a letter of credit. The necessity for the seller to trust the buyer is removed. The seller is made sure of payment and the buyer is sure of receiving documents. It is for these reasons that banks will only agree to issue such instruments for creditworthy applicants and after satisfying themselves of creditworthiness and security considerations.

The Seller, however, has the responsibility of assessing the level of reliance he places upon the issuing bank and the political stability of the country concerned. From the viewpoint of the buyer, while the seller must produce conforming documents with the Letter of Credit, the buyer will still be reliant upon the standing of the supplier and their ability to manufacture/ship goods in terms of the quality required.

There is a contract of sale between the buyer and the seller, under which the parties stipulate the documentary credit as the method of payment and undertake to perform certain obligations for the purpose of giving effect to the documentary credit. There is a contract of reimbursement or similar agreement between the applicant, the buyer, and the issuing bank, under which the issuing bank agrees to provide a documentary credit and the applicant undertakes to reimburse the bank and compensate its loss if necessary. There is a contractual undertaking between the beneficiary, the seller, and the issuing bank, under which the issuing bank promises or guarantees the payment to the beneficiary provided that he fulfills the obligations under the credit.

When the issuing bank deals with the beneficiary, the seller, directly, there would be an agent principal arrangement between the issuing bank and the nominated bank, i.e., an advising bank, negotiating bank or confirming bank, under which the issuing bank undertakes to reimburse and compensate the nominated bank for its services and the nominated bank undertakes to act as instructed by the issuing bank. If a nominated bank confirms the credit, there would be a contractual undertaking between the confirming bank and the beneficiary, under which the confirming bank guarantees the payment of the credit provided that the beneficiary performs the terms of the credit.

In considering the liability between the issuing bank and the confirming bank in case of non conforming documents, the English Court held that the Uniform Custom Practices required the issuing bank to examine the documents as they were and did not allow the issuing bank to send them to the buyer for the purpose of identifying the discrepancies. In bankers Trust Co. V State bank of India (1991) 2 Lloyds Rep 443 the Bankers Trust failed to comply with the requirement to give timely notice to the negotiating bank of the alleged discrepancies and the negotiating bank was held entitled to claim reimbursement from the State Bank of India.

In the instant case, the issue to be considered is whether the Appellant bank which negotiated the letters of credit, has recourse against the seller, in this case the Respondent for recovery of the monies paid on the said letters of credit. The learned High Court judge held that the Appellant cannot recover from the Respondent, and can only proceed against the Issuing Bank, despite finding that the monies had been paid by the Appellant bank to the Respondent upon negotiating the letters of credit.

The Appellant banks position is that the above transaction is akin to a loan transaction. It is settled law that the Appellant Bank could either sue the Principal borrower or the guarantor or any of them. In the instant case the Appellant bank clearly has a right of recourse for payment of monies due under the Letter of Credit from the issuing bank (the principal). The Appellant bank also has a right of recourse against the Respondent as the seller, for recovery of the sums due. Therefore this court finds that based on the guarantees furnished by the Respondent, the Plaintiff may proceed against the Issuing Bank and/or the Respondent, but cannot under any circumstance recover from both.

The Respondent has also claimed that the Appellant Bank cannot maintain this action since the Plaint does not disclose a cause of action in terms of the guarantees but only on letters of credit. The Appellant banks position is that the action was instituted on the contractual agreement between the Appellant and the Respondent, which is based on the guarantees furnished by the Respondent marked P10 and P11. In considering the submissions of both parties, this Court finds that the action has been instituted based on the guarantees of the Respondent and not on the letters of credit.

The Respondents took up the further position that the Appellant Bank could not have instituted the action pending a final ruling on the dispute by the International Chamber of Commerce (hereinafter referred to as the ICC). The learned High Court judge relied on the contents of document P9 which provides that 'arrangements are underway to obtain a ruling from the ICC regarding the accuracy of the clean unpaid L/C bills...the total value of these two bills plus the interest will be held separately until a ruling is received in this regard'. The Appellant bank relied on the undertaking by

the Respondent to reimburse the Appellant unconditionally the monies due in terms of the said Letters of Credit together with the interest and other charges thereon and the specific waiver of all the Respondent's right to contest the amount or nature of the claim of the Appellant in respect of amounts paid by the Appellant under the guarantee (Vide, P10, P11).

The learned High Court judge in page 08 of the judgment speculates that the Appellant may be unjustly enriched where the company recovers the monies from the Respondent and on subsequently the Issuing Bank makes the due payment to the Appellant. However in the instant case, this Court finds that while the Appellant bank has a right of recourse against the Issuing bank and also against the Respondent, it may not under any circumstance recover from both. Therefore the issue of unjust enrichment of the Appellant bank does not arise in this case.

Under these circumstances this Court holds in favor of the Appellant bank and sets aside the judgment of the learned High Court Judge of the Commercial High Court Colombo dated 10.06.2004 and orders the Respondent to pay the Appellant bank the total monies as prayed for in the Plaint before the Commercial High Court which is;

a) In a sum of US \$ 527,874/61 together with interest at the rate of 9% per annum on a sum of US \$ 347,972/72 from 01.10.2001 until date of Decree and thereafter legal interest on the decreed sum until payment in full together with statutory charges there on.

b) In a sum of US \$ 288,163/16 together with interest at the rate of 9% per annum on a sum of US \$ 187,324/94 from 01.10.2001 until date of Decree and thereafter legal interest on the decreed sum until payment in full



together with statutory charges there on.

Accordingly the Appeal is allowed with costs payable by the Respondents to the Appellant bank in a sum of 50,000/-

**JUDGE OF THE SUPREME COURT**

**Ekanayake, J.**

I agree.

**JUDGE OF THE SUPREME COURT**

**Dep, PC, J.**

I agree.

**JUDGE OF THE SUPREME COURT**