

HOW RELIABLE IS A PAYMENT LOI?

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The high-profile failures of a number of oil traders including Hin Leong Trading (Pte.) Ltd (“Hin Leong”) and ZenRock Commodities Trading Pte Ltd (“Zenrock”) have led to a spate of court decisions relating to the fallout. The focus of commentary on those decisions has largely been on whether the fraud exception has been engaged to enable the relevant bank to resist payment under a letter of credit (“LC”). See our earlier article on false representations in letters of credit: key developments in Singapore.

"Marketable title was title that may at all times and under all circumstances be forced on an unwilling buyer in contrast to a title which would expose the buyer to litigation or hazard."

In this article, we focus on the use of payment letters of indemnity (“Payment LOI”) that are presented in place of the original bills of lading under the LC and whether the buyer and/or bank can rely on them.

There is no set wording for a Payment LOI but it usually:

- records the agreement to make payment to the seller;
- provides consideration for the payment obligation;
- gives a warranty (of some or all of the following) at the time property passed under the sale contract alternatively on delivery of cargo to the buyer that (a) the seller has good/marketable title to the cargo; (b) the cargo is free and clear of any lien or encumbrance; (c) the seller has the right to transfer title to the buyer; (d) the seller is entitled to receive the documents from its supplier; and (e) the seller will deliver the original bills to the buyer; and
- provides an indemnity for breach of any of the warranties or for the consequences of the original bills remaining outstanding.

Three decisions have put the spotlight on what reliance can be placed on a Payment LOI by a buyer or the issuing bank under a LC: *Winson Oil Trading Pte Ltd (“Winson”) v OCBC and Standard Chartered Bank (Singapore) Limited (“SCB”) (2023) SGHC 220*, *Credit Agricole Corporate Investment Bank (“CACIB”) v PPT Energy Trading Co Ltd (“PPT”) (2023) SGCA(I) 7* and *Unicredit Bank AG v Glencore Singapore Pte Ltd (2023) SGCA 41*.

SOME COMMON THEMES

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In all three decisions, Payment LOIs were presented instead of the original bills. In Winson the LOIs were issued to Hin Leong as Winson's buyer. In Credit Agricole, the LOI was issued by PPT to CACIB and in Unicredit, the LOI was issued by Glencore to Hin Leong.

In each case, the bank in question was seeking to resist payment under a LC on the basis of the fraud exception coupled with other defences. In Winson, the LOIs were based on non-negotiable copies of the bills which were held to be forgeries and it was argued in addition that the LOIs were nullities since no cargo had been shipped under the sale contract between Winson and Hin Leong. In CACIB, the bank claimed that PPT was in breach of the warranties given in the LOI and liable to pay damages equivalent to the sum that PPT sought from CACIB under the LC. In Unicredit, the bank contended that in presenting the LOI, Glencore represented that it intended to locate and surrender the bills.

Winson

In the LOIs given by Winson it warranted that the bills existed, it had good title and had passed good title back to Hin Leong. The court held that since the non-negotiable copies of the bills were forgeries, it followed that there were no valid bills pursuant to which the cargo was shipped and thus Winson's representations to the banks as to the existence and validity of the bills were false. In addition, there were no loading documents for the cargo purportedly sold by Winson to Hin Leong, thus the representation that such cargo had been shipped on the vessels named in the bills was also false (as was the representation that Winson had good title to those cargoes and had passed good title to Hin Leong).

CACIB

PPT warranted in the LOI that it had a marketable title to the cargo free and clear of any lien and encumbrances and gave an indemnity in favour of the bank against all damages, costs and expenses which the bank might suffer if the original bills of lading remained outstanding or there was a breach of warranty.

The Court of Appeal disagreed with the judge at first instance who was of the view that the LOI was a unilateral contract which could only be accepted by the bank if it paid the specified price under the LC by the due date. It held that the LOI was effective from the time that it was issued and the real question was whether payment by the due date under the LC was a condition precedent to PPT's obligation to indemnify the bank under the LOI. The court saw no need to construe the reference to due date as a strict condition but instead, referring to *Spar Shipping AS v Grand China Logistics Holding (Group) Co Ltd* [2016] EWCA Civ 982, viewed it as an innominate term.

More interestingly, the Court of Appeal disagreed with the High Court's view that title had passed in the ordinary way on shipment and that the expression "marketable title" added nothing to the obligation that the title be free and clear of any lien or encumbrance. It held that marketable title was title that may at all times and under all circumstances be forced on an unwilling buyer in contrast to a title which would expose the buyer to litigation or hazard.

The Court of Appeal considered that the High Court had been in error in construing “marketable title” as being synonymous with the implied term in sale of goods legislation that the goods are free from any charge or encumbrance, which is regarded as a warranty sounding only in damages. On the contrary, the warranty in the LOI was not a warranty of the UK Sale of Goods Act 1979 variety. Rather, the title held by PPT was of uncertain value in circumstances where due to the fraud, the floating charge given to the bank had crystallised prior to the sale. The court considered that there were well-founded concerns about the marketability of the title held by PPT.

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Unicredit

Hin Leong agreed to buy fuel oil from Glencore and Glencore agreed to immediately sell it back to Hin Leong. Unicredit issued a LC in favour of Glencore to finance Hin Leong's purchase which permitted payment to be made against Glencore's Payment LOI. Unicredit remained unaware that Glencore had bought the cargo back until after Hin Leong had become insolvent and was unable to reimburse the bank.

The bank failed at first instance in all its claims, but on appeal, focusing on the relevance of the Payment LOI, Unicredit argued that by tendering its invoice and Payment LOI, Glencore made the representation that it intended to locate and surrender the bills of lading and that it did so either knowing that was false or without any genuine belief that it was true.

Crucially, the Court of Appeal concurred with the High Court that the tender of the LOI did not give rise to any representation that Glencore had agreed to locate and surrender the bills of lading to Hin Leong. The LOI was addressed to Hin Leong not Unicredit and the court took the view that by not requiring the LOI to provide that the bills be delivered to the bank, the latter accepted the risk that came with not so providing. Unicredit was attempting to muscle in on a contractual obligation made between Glencore and Hin Leong and trying to rely on a contractual promise to which it was not privy.

Unicredit argued that since there had been a buyback, Glencore would never be in a position to deliver bills of lading to Hin Leong. In construing the LOI, the court pointed out that it contemplated that the underlying transaction was one in which bills might never be delivered. It was on this basis that Glencore undertook to indemnify Hin Leong against any losses which resulted, so there was no implied representation on the part of Glencore even to Hin Leong that it intended to locate and deliver the bills to it.

Importantly, Glencore itself had opened an LC in favour of Hin Leong in respect of the buyback which permitted Hin Leong to present a Payment LOI to Glencore's bank, Banco Bilbao Vizcaya Argentaria ("BBVA"), which it did. BBVA could therefore have demanded the bills from Hin Leong and if this happened Hin Leong would have had to ask Glencore for them. It could not be said therefore that Glencore knew that Hin Leong would never ask for the bills.

CONCLUSION

In presenting an LOI, an issuer may be taken to have implied certain representations beyond those expressly made such as the actual loading of the cargo on the named vessel. It may be prudent for an issuer to try to limit representations expressly to those set out in the LOI.

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From the recipient's perspective, good or marketable title in this context is different from the implied term in the UK Sale of Goods Act 1979, which imposes a condition of the right to sell and warranties of quiet possession and freedom from lien or encumbrance. In CACIB, reference was only made to the warranty relating to lien or encumbrance. The broader definition of marketable title adopted in CACIB is based on real property where the buyer is entitled to be satisfied that the seller is in a position, without the possibility of dispute or litigation, to pass that title to the buyer.

There is some uncertainty about whether a bank can rely on representations made in a LOI not addressed to it but to the buyer and vice-versa. In Winson, the court appears to have assumed that representations as to the existence and validity of the bills could be relied on by the banks even though the LOI was addressed to Hin Leong. In contrast in Unicredit, the Court of Appeal held that representations made to Hin Leong could not be relied on by the bank given that the LOI was addressed to Hin Leong. The court commented that the bank could have insisted that the LOI state that the bills be delivered to the bank, but it did not, so it assumed the risk.

Thus, an issuing bank will be advised to ensure the LOI presented under the LC is addressed to them (or at the very least to them and the buyer) and that there is an express obligation to deliver up the bills to them once received by the seller in order to overcome the issue of whether such a representation is capable of being implied.

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