

- SUBJECT:** Revising statutes governing letters of credit
- COMMITTEE:** Financial Institutions — favorable, without amendment
- VOTE:** 7 ayes — Averitt, Solomons, Denny, Ehrhardt, Elkins, Marchant, Juan Solis
0 nays
2 absent — Grusendorf, Pitts
- WITNESSES:** For — W. David East, Texas Business Law Foundation
Against — None
- BACKGROUND:** Chapters 1-9 of the Business and Commerce Code conform to the Uniform Commercial Code (UCC), which nearly every state, including Texas, has adopted. The UCC governs commercial transactions, including commercial paper, leases, transfers of funds, bank deposits, bills of lading, and letters of credit. In 1995, the American Law Institute and the National Conference of Commissioners on Uniform State Laws, the drafters of the UCC, proposed many revisions to Article 5 of the UCC, relating to letters of credit. Letters of credit assure the credit-worthiness of individuals and facilitate certain financial transactions, particularly in international trade.
- DIGEST:** HB 366 would revise Chapter 5, Business and Commerce Code to conform to the 1995 UCC revisions. Specifically, HB 366 would:
- codify the Independence Principle, under which a financial institution involved in a letter-of-credit transaction is generally independent of the transaction itself;
 - expand the scope of Chapter 5 to include all letters of credit;
 - allow a letter of credit to be issued in any form that is an authenticated record, including via electronic means;
 - update issuance, amendment, cancellation, and duration provisions related to letters of credit to be consistent with modern commercial practices;
 - define terms to be consistent with the UCC and with other states' laws;
 - provide issuer's rights and obligations, including obligations to honor fraudulent documents that appear proper;

- prescribe remedies for wrongful dishonor of a letter of credit and for fraud;
- state the terms by which a letter of credit could be transferred;
- establish a one-year statute of limitations;
- define requirements for choice of law and choice of forum;
- allow subrogation of the rights of issuers, applicants, and nominated persons;
- clarify that warranties do not arise until a letter of credit is honored; and
- make awards of reasonable attorney's fees permissive rather than mandatory.

HB 366 would take effect September 1, 1999.

**SUPPORTERS
SAY:**

HB 366 would update Texas law regarding letters of credit to reflect current commercial practices and the advent of electronic commerce. This would be the first major revision to Chapter 5 since its adoption in 1967. Since 1995, 39 states have revised their statutes in accordance with the UCC changes recommended by the American Law Institute and the National Conference of Commissioners on Uniform State Laws.

Because many international letters of credit are modeled on the uniform language, revising the statute would reduce inconsistencies between Texas and other states and would decrease the likelihood that a letter of credit inadvertently would violate provisions of state law. Also, HB 366 would replace arcane requirements — such as that the letter of credit be in written form and signed — that electronic commerce has supplanted.

The Independence Principle is an important aspect of commercial transactions and needs to be written in statute. Although case law recognizes this principle, state law does not define it, leaving open the possibility that case law will not always adhere to the principle.

**OPPONENTS
SAY:**

No apparent opposition.

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NOTES: The companion bill, SB 85 by Carona, identical to HB 366, passed the Senate by voice vote on February 25. The House Financial Institutions Committee reported SB 85 favorably without amendment on March 15.

SB 547 by Carona, a substantially similar bill, passed the Senate by voice vote during the 1997 regular session, but died in the House when all bills on the May 27, 1997, House calendar were ruled out of order.