Selected Judgment No.10 of 2019
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IN THE SUPREME COURT OF ZAMBIA **APPEAL NO.123/2016**
HOLDEN AT LUSAKA **SCZ/8/36/2016**
(CIVIL JURISDICTION)

BETWEEN:

KV WHEELS AND CONSTRUCTION LTD	**1ST APPELLANT**
MORGAN KASEBA	**2ND APPELLANT**
ANDERSON KANSILYE SIMWINGA	**3RD APPELLANT**
HENRY CHANZA SIMUYEMBA	**4TH APPELLANT**
KENNEDY NONDE SIMWINGA	**5TH APPELLANT**
SANDRA LUCHEMBE SIMWINGA	**6TH APPELLANT**

AND

DEVELOPMENT BANK OF ZAMBIA	**RESPONDENT**

CORAM: Musonda, Ag.D.C.J, Hamaundu, and Wood JJS
On the 5th October, 2016 and 28th March, 2019

For the Appellants : Mr M. Mutemwa Sc, Messrs Mutemwa Chambers and Capt. B.A. Sitali, Messrs Butler & Partners

For the Respondent : Mrs N. Mumba, Legal Counsel

JUDGMENT

Hamaundu, JS delivered the Judgment of the court.

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Works referred to:

1. **Schmitthoff's Export Trade: The Law and Practice of International Trade, 11th edition, Thomson Reuter, London, 2007**
2. **The Law of International Trade, 7th edition, HLT Publications, London, 1996**

This appeal is against a judgment of the High Court which granted the respondent's mortgage action against the appellants. The facts that were presented before the court below were these:

The 1st appellant being desirous of setting up a plant that would enable it make concrete blocks and pavers, obtained finance from the respondent. A loan agreement was signed in which the 1st appellant obtained a medium-term loan for the purchase of the equipment and another loan as working capital. The loans were secured by a range of securities that included charges on the 1st respondent's assets, third party mortgages and a guarantee from the Directors. That is how the other appellants came to be parties to this action.

The manufacturer/supplier of the equipment was paid. The machinery however was supplied in batches over a period of two to three years. There was no dispute that the 1st appellant defaulted on its repayments as stipulated in the loan agreement. When the respondent commenced this mortgage action, the defence by the

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appellants was that the 1st appellant had defaulted on its repayments because the project for which the money had been borrowed had not taken off the ground; the appellants attributed this to the failure by the manufacturer to supply all the machinery at once.

The appellants went a step further and accused the respondent of negligence. According to the appellants, this arose from the fact that, contrary to the terms of the letter of credit, the respondent paid the manufacturer without satisfying itself that all the equipment was reflecting on the shipping documents sent by the manufacturer. The appellants also accused the respondent of failing to pursue the manufacturer in order to ensure that the machinery was supplied in time. Consequently, the appellants argued that, by those omissions, the respondent had induced the default and could therefore not be entitled to claim the reliefs it sought.

The respondent counter-argued that it was not its responsibility to ensure that the manufacturer supplied all the machinery. The respondent went on to contend that, in any case, it authorized the payment after satisfying itself that the equipment that was listed on

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the shipping documents matched the equipment listed on the invoice.

The main issue that the trial court identified as the one for determination was whether, in the light of the two contentious positions, the respondent was entitled to enforce its rights under the loan agreement and the security documents.

The trial court examined the two facility letters issued by the respondent, which comprised the loan agreement between the respondent and the 1st appellant. The court also examined the security documents; namely the mortgages, charge, debenture and guarantee. The court noted that the loan agreement set out the repayment terms, and that both the loan agreement and the security documents had one clause in common: the default clause which provided for payment of all monies due, and gave the right to possession and sale of the charged properties in the event of default. The court held that the parties in this case had bound themselves within the four corners of the loan agreement and that, it being undisputed that the 1st appellant had defaulted, the respondent was

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entitled to invoke the default clause in the loan agreement and the other security documents. In the court's view, the appellants could not be heard to justify the default by alleging that the respondent had triggered the default because; first, the loan agreement and the agreement for the supply of the machinery were two separate contracts which were not subject to each other. Secondly, the loan agreement contained an entire agreement clause which meant that the parties could only refer to the terms in that agreement and not elsewhere; and, thirdly, the respondent was not a party to the contract for the supply of the machinery. To arrive at this last conclusion, the court looked at the invoices that were issued by the supplier and noted that they were all addressed to the 1st appellant. The court also looked at the Bill of lading and the packing list and noted that; in the first document, the 1st respondent was referred to as the party to be notified while Investrust Bank Plc was referred to as the Consignee; in the second document, the court noted that the supplier was referred to as the issuer of the document while the

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document itself was addressed to the 1st appellant. The court found as a fact that in neither of these documents was the respondent mentioned. Accordingly, the court held that the respondent could neither benefit nor be held liable under the supply contract.

The court then considered the argument by counsel for the appellants that the transaction between the respondent and the appellant was subject to the **Uniform Customs and Practice for Documentary Credits Rules (UCP 600)** with regard to the letter of credit. The court decided to examine the **UCP rules**. We must mention here that this whole appeal is based on the court's findings upon its interpretation of these rules. First, the court examined the letter of credit and found that it did incorporate the **UCP rules**. The court, therefore, dismissed the respondent's argument that the **UCP rules** did not apply to the letter of credit. The court then went on to consider the arguments by the appellants that under the **UCP rules** the respondent was bound to ensure that all the capital assets and equipment were delivered before it authorized payment to the

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supplier; and that the respondent was also duty-bound to follow up with the supplier when the under-delivery of the capital assets and equipment was noticed. Consequently, the court examined the articles in the **UCP rules** that were referred to it by the appellants. It noted that **article 4** provided that a credit by its nature is a separate transaction from the sale or other contract; and that banks are in no way concerned with or bound by such contract, even if any reference whatsoever to it is included in the credit. The court then looked at the definition of some of the terms in the **UCP rules** as they are defined in **article 2**. For example; "applicant" is defined as the party on whose request the credit is issued; *"beneficiary"* is defined as the party in whose favour the credit is issued; *"advising bank"* is defined as the bank that advises the credit at the request of the issuing bank. Applying these definitions to the parties that were involved, the court assigned the term *"applicant"* to the 1st appellant. The term *"beneficiary"* was assigned to the supplier. The term *"advising bank"* was assigned to the respondent. The term *"issuing bank"* was

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assigned to Investrust Bank Plc. The court fortified its assignment of the term *"advising bank"* by the definition of that term in **Blackie's Dictionary of Banking,** which is that it is the bank that advises a beneficiary, an exporter, that a letter of credit has been opened by an issuing bank. As will be seen, it is this assignment of the terms which is at the core of this appeal. The court then held that by the provisions of **article 4** the respondent was not concerned with the sale of the equipment. According to the court below, the provisions of **article 4** tallied with its earlier finding that the respondent was not a party to the sale transaction involving the capital assets and equipment; and that that transaction was separate from the credit contract.

The court then examined **article 14** and found that the duty to examine documents prior to payment fell on to the *"issuing bank"*. The court found that it was not the role of the *"advising bank"* to do so. Consequently, the court held that it was not the respondent's duty, as *"advising bank"*, to examine the documents, although in this

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case the respondent did examine them; and that, having nevertheless examined the documents, the respondent's duty ended at just that. The duty did not extend to inspecting the assets and equipment as contended by the appellants. With that reasoning, the court below found, as untenable, the appellants arguments alleging negligence and inducing the default on the part of the respondent.

The court therefore granted the reliefs sought by the respondent.

The appellants appeal on three grounds as follows:

1. **that the learned judge in the court below erred in law and fact when he held that the respondent was an advising bank**
2. **that the learned judge in the court below erred in law and fact when he held that the respondent had no obligation to inspect the documents presented by the seller for compliance with the terms and conditions of the letter of credit: and**
3. **that the learned judge in the court below misdirected himself when he ignored the evidence showing that the appellant's failure to service the loans was a direct result of the respondent's default in making payment on documents which were not compliant with the terms of the letter of credit and the order.**

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As can be seen from these grounds, the only issue in this appeal is the classification of the respondent in the transaction: was it an *"advising bank"* or an *"issuing bank"*, or neither of the two. This issue is raised in the first ground. The further consideration of the second and third grounds of appeal will depend on the outcome of the 1st ground of appeal. For example, the court below found that the **UCP rules** place the duty of inspecting documents presented by the seller on the *"issuing bank"*. So, if we do agree in the first ground with the court below that the respondent was not an *"issuing bank"* then both grounds two and three must automatically fail.

The arguments by the appellants in the first ground of appeal were that; first, Investrust Bank was not an agent of the 1st appellant but that of the respondent. According to the appellants, this was evidenced by the fact that Investrust Bank issued the letter of credit on the instructions of the respondent; and that, even when it came to payment, it was the respondent that authorized Investrust Bank to pay.

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Secondly, learned counsel for the appellant argued that, contrary to the holding by the court below, the respondent was not the *"advising bank"*; and neither was Investrust bank the *"issuing bank"*. According to learned counsel, an advising bank would typically be located in the same country as the exporter or the beneficiary of the letter of credit. In this case, it was argued, the respondent was not situate in Italy where the seller is domiciled. Counsel also argued that it was not the respondent that advised the seller that the letter of credit was available. It was argued that, in this case, the respondent was ultimately responsible for payment to the supplier; and was the one which decided the terms and conditions of the letter of credit. We were referred to the definition of a *"nominated bank"* as defined in **article 2** of the *UCP 600* rules which states:

> **"the bank with which the letter of credit is available or any bank in the case of a credit available with any bank".**

Counsel argued that, in this case, Investrust Bank was the bank with which the letter of credit was available and, therefore, it was the

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nominated bank. As for the respondent, counsel argued that it was the one that bore the liability to pay or honour the letter of credit; meaning that it was the *"issuing bank"*.

In response, counsel for the respondent submitted that the dispute in this matter arises solely from the appellants' misunderstanding of the nature and mechanism of letters of credit. With the aid of decided cases and academic works, learned counsel endeavoured to explain the mechanism of letters of credit. Two of those authorities are very important to the resolution of the first ground of appeal. Counsel quoted a passage from the works: **Schmitthoff's Export Trade: The Law and Practice of International Trade**[2], (*paragraph 11-005*) where the authors set out four stages of a letter of credit transaction. The passage reads thus:

> **"Where payment under a letter of credit is arranged four stages can normally be distinguished.**
>
> **(a) The exporter and the overseas buyer agree in the contract of sale that payment shall be made under a letter of credit.**
>
> **(b) The overseas buyer (acting as 'applicant for the**

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credit') instructs a bank at his place of business (known as 'the issuing bank') to open a letter of credit for the .... Exporter (known as 'the beneficiary') on the terms specified by the buyer in his instructions to the issuing bank.

(c) The issuing bank arranges with the bank at the locality of the exporter (known as the 'advising bank') to negotiate, accept or pay the exporters draft upon delivery of the transport documents by the seller.

(d) The advising bank informs the exporter that it will negotiate, accept or pay his draft upon delivery of the transport documents. The advising bank may do so either without its own engagement or it may confirm the credit opened by the issuing bank".

Counsel then quoted passages from the works, **Law of International Trade,** edited by **P. Sellman**[3], under the heading *"The Parties" (Section 4.3, pages 126-129)* where the editor sets out the parties to a letter of credit transaction and their roles. The passages read:

"the parties to the Documentary Credit Arrangement are as follows:

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The applicant for the credit

This is the buyer under the contract of sale, by whom the contractual price is owed... the instructions given by the buyer to his bank will reflect the sale contract between himself and the seller.....

The issuing bank

When the bank of the buyer is in receipt of the buyer's instructions, it will issue notice to the seller that the credit has been opened and the conditions with which the seller must comply in order to obtain payment under the credit. This is referred to as the issuing bank.

The issuing bank gives an undertaking, as principal, to pay against correct documents in accordance with the mandate of the buyer..... The issuing bank may communicate the opening of the credit to the seller direct or via the mediation of another bank which is situated in the seller's country of residence. This is referred to as the correspondent or advising bank.....

The correspondent bank

The correspondent bank may assume one of two capabilities, first as adviser and, secondly, as confirmer.

The correspondent adviser

Where a correspondent bank is used as an adviser, it does not assume any undertaking to make payment to the beneficiary on its own behalf. Its purpose is merely to advise the beneficiary of the terms with which he must comply if he is to receive

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> **payment from the issuing bank. Its involvement merely facilitates the communication of the credit terms.....**
>
> **<u>The correspondent confirmer</u>**
>
> **Where the correspondent bank confirms the credit facility, not only does it communicate to the seller that the credit has been opened in his favour but gives him a complete, separate and additional undertaking to make payment if correct documents are tendered to it.....**
>
> **<u>The beneficiary</u>**
>
> **The beneficiary under the documentary credit is the seller under the contract of sale...."**

Counsel submitted that in this case there was a letter of credit transaction which fulfilled all the stages explained above. We were referred to the *SWIFT MT 700* message on the record of appeal which comprised the letter of credit. Counsel pointed out that the said letter of credit showed that the 1st appellant was indeed the *"applicant"* and the supplier was the *"beneficiary"*. She further pointed out that, according to the letter of credit, the *"issuing bank"* was Investrust Bank and that the letter of credit was notified to Citi Bank US who confirmed it. Counsel also referred us to the Bill of lading and the

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commercial invoice which also showed that Investrust Bank was the *"issuing bank"*. Counsel submitted that, from the letter of credit, Citi Bank was the *"correspondent confirming bank"*; meaning that, instead of being merely advisory, it had undertaken to make payment as well. On that ground counsel disagreed with the holding by the court below that the respondent herein was the *"advising bank"* because that role was for Citi Bank US which went beyond *"advising"* and took up the role of *confirming*. Counsel then submitted that the respondent herein was merely a party to the loan transaction between it and the 1st appellant; and that, pursuant to that transaction, the respondent undertook to provide cash cover on behalf of the 1st appellant for the amount covered by the letter of credit. Counsel argued that, in those circumstances, the fact that the respondent was in contact with Investrust Bank directly and that it even inspected documents is indicative only of the fact that it was trying to secure its interests as financier under the loan transaction.

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We are in total agreement with the explanation by the respondent as regards the parties to a letter of credit transaction; and their roles therein. It is clear from the authorities cited, and indeed the letter of credit itself that the *"issuing bank"* in this case was Investrust Bank. It is also clear from the authorities that the loan agreement between the respondent and the 1st appellant was separate from the sale of goods contract between the 1st appellant and the supplier; so that the respondent could not be expected to perform any part of the latter contract, and be held liable for breach of any obligations thereunder. Hence, the court below was on firm ground when it so held.

We said at the beginning that this appeal revolved mainly around the question whether the respondent was an *"advising bank"* or an *"issuing bank"*. The authorities and letter of credit have shown that it was neither of the two. It follows that whatever liability the appellants would like to attach to the respondent cannot be so attached. It also follows that there can be no further consideration of

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the second and third grounds of appeal. We therefore find no merit in this appeal.

The appeal shall stand dismissed, with costs to the respondent.

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M. Musonda
ACTING DEPUTY CHIEF JUSTICE

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E. M. Hamaundu
SUPREME COURT JUDGE

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A. M. Wood
SUPREME COURT JUDGE