

Sanctions Clauses under Singapore Law: An Objective Inquiry, and Validity Questioned

Client Alert | October 11, 2023

Singapore's highest court rendered decision in *Kuvera Resources Pte Ltd v JPMorgan Chase Bank, N.A.* [2023] SGCA 28, holding that the interpretation of a sanctions clause in the context of a letter of credit was to be strictly and objectively construed. In this case, the court held that the bank's concern of a potential adverse finding by the US Office of Foreign Assets Control ("OFAC") did not suffice to excuse it from paying on an otherwise complying presentation. The court further expressed doubt as to whether such a clause was compatible with the commercial purpose of a letter of credit.

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Background Facts

In 2019, a contract for the sale of coal to be delivered in two shipments was entered into between an Indonesian seller and a UAE buyer. The appellant, Kuvera Resources Pte Ltd, had advanced funds to the seller to purchase coal for on-selling to the buyer and was the beneficiary of two irrevocable letters of credit payable at sight ("the LCs"). Both LCs were issued by a bank in Dubai, subject to the Uniform Customs and Practice for Documentary Credits, 2007 Revision ("UCP600"). JPMorgan ("the Bank") was the advising and nominated bank for both LCs.

At the time, all of the Bank's advices and confirmations contained a sanctions clause in the following terms:

[The Bank] must comply with all sanctions, embargo and other laws and regulations of the U.S. and of other applicable jurisdictions to the extent they do not conflict with such U.S. laws and regulations ("applicable restrictions"). Should documents be presented involving any country, entity, vessel or individual listed in or otherwise subject to any applicable restriction, we shall not be liable for any delay or failure to pay, process or return such documents or for any related disclosure of information.

Kuvera subsequently made complying presentations to the Bank, which were then screened for potential sanctions issues. It transpired that the vessel in this case was on an internal list maintained by the bank, on the basis that it might have been Syrian-owned despite its non-Syrian registration. The Bank's list was different to the list published by OFAC on its website, as it included other entities that the Bank had determined had known businesses in sanctioned countries. On the basis of the vessel being on the Bank's list, it declined to pay on the LCs.

The Decision

Interpretation of the sanctions clause

The Court of Appeal, which is Singapore's highest court, found that the sanctions clause

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did not afford a basis to decline payment. The court held that the sanctions clause only permitted the bank to decline payment if the vessel was “listed in or otherwise subject to any applicable restriction.” The vessel, not being listed by OFAC and only in the bank’s internal document, did not qualify as having been “listed in...any applicable restriction.” The court then considered whether the vessel might be said to be “otherwise subject to any applicable restriction.”

The court rejected a subjective approach to this question, finding that it did not suffice even if it could be shown that OFAC may or would have found that paying Kuvera was a breach of US sanctions; nor did it matter that the Bank was reasonably concerned that making payment could or would have been found by OFAC to be a breach of US sanctions.

Instead, an objective approach was required. Accordingly, the only relevant question was whether, as a matter of objective determination, the vessel had been Syrian-owned at all material times.

The court explained that:

(a) Allowing a nominated bank to decline payment based on what OFAC (which was not identified in the sanctions clause) may eventually find was considered arbitrary and speculative. This did not afford a beneficiary any certainty as to payment. The court noted evidence that the OFAC process itself was elaborate and long-drawn.

(b) The list maintained by the Bank reflected its own judgment, and an entity could be listed even if the risk of violation of US sanctions was less than even. The court went on to opine that even the presence of ‘red flags’ surrounding the ownership of the vessel, but which could not be resolved entirely, did not suffice to demonstrate that the vessel was in fact subject to an applicable restriction.

(c) Even though there was correspondence with OFAC that resulted in OFAC opining that there would have been “an apparent violation of OFAC regulations” based on information provided by the Bank, the court viewed the request as seeking support from OFAC for a decision the Bank had already made.

The court went on to analyze the evidence put forward on the ownership of the vessel and found it insufficient to displace the presumption of ownership arising from the vessel’s non-Syrian registration. Accordingly, the Bank was unable to discharge its burden of justifying its non-payment.

Whether sanctions clauses are enforceable

The court accepted that additional conditions stipulated in a confirmation could be binding and need not be separately offered and accepted so long as they did not contradict the commercial purpose of the LCs. In this regard, the court expressed doubt whether the sanctions clause in question was inconsistent with the commercial purpose of the LCs, particularly in a situation concerning the nomination of a vessel. This was because the beneficiary would not be involved in nominating the vessel, and therefore would have no knowledge at the time of contracting whether the letter of credit would be enforceable.

The court also noted the lack of any direct authority expressly upholding the validity of a sanctions clause in the context of UCP600 or documentary letters of credit generally. While there was English authority recognizing sanctions clauses, these were in respect of general commercial transactions. The court was particularly focused on the fact that letters of credit had a unique characteristic as autonomous contracts, and that confirmations (which, in this case, contained the sanctions clause) were often unilateral and would not have been negotiated or agreed by the beneficiaries.

Lessons

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The primary takeaway from this decision is that, at least under Singapore law, a sanctions clause will be construed strictly and objectively. If greater discretion is desired to decline payment based on an internal assessment by the bank, or even correspondence with OFAC, this needs to be spelt out clearly in the clause.

However, the greater the discretion afforded to decline payment, the greater the likelihood the court may also find the sanctions clause to be incompatible or inconsistent with the purpose of the letter of credit, which is to give the beneficiary "an assured right to be paid". It may be that a sanctions clause agreed to by the parties to the underlying transaction, including the beneficiary, would be viewed more favorably. This, of course, changes how such transactions are presently carried out.

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Gibson Dunn's lawyers are available to assist in addressing any questions you may have regarding these developments. Please contact the Gibson Dunn lawyer with whom you usually work, any member of the firm's International Arbitration, International Trade, or Financial Institutions practice groups, or any of the following:

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