

ALASKA LEGISLATURE COMMITTEE FILES 1997-1998 86/2

9303 HOUSE LABOR & COMMERCE

Representative Norman Rokeberg

March 13, 1997

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An "adviser" is a person who notifies the beneficiary (or another "adviser" who will notify the beneficiary) that a letter of credit has been issued, confirmed, or amended.

This bill revises the rules that set up how letters of credit work and the relationships between all of the various parties involved.

**Section 1.** AS 09.30.070(b). Makes an amendment conforming this subsection to proposed AS 45.05.111(d). This bill section deals with interest on a court judgment and establishes when interest starts accruing before the judgment is handed down. Under AS 45.05.111(d), interest on money owed for a liability found under AS 45.05.111(a) - (c) starts when the letter of credit is wrongfully dishonored or on another appropriate date.

**Section 2.** AS 45.01.105(b). Makes an amendment conforming this subsection to the proposed AS 45.05 changes. AS 45.01.105 identifies which state or nation's law governs in certain cases involving more than one state or nation. The amendment states that AS 45.05.116 establishes what law governs for letters of credit.

**Section 3.** AS 45.02.512(a). Makes an amendment conforming this subsection to proposed AS 45.05.109(b). Excuses a buyer from making payment, even if the contract requires payment before inspection and the required documents are tendered, if the circumstances would justify an injunction under AS 45.05.109(b).

**Section 4.** AS 45.05.102. Defines the terms used in the revised chapter on letters of credit (AS 45.05). See the introductory comments to this memo for more simple definitions of the most important terms.

**Section 5.** AS 45.05.103. Defines the scope of AS 45.05.

AS 45.05.103(a). States that the chapter applies to letters of credit and transactions involving letters of credit.

AS 45.05.103(b). States that this chapter, by itself, does not govern how to treat another situation or person not covered by this chapter.

AS 45.05.103(c). States that you can change the provisions of this chapter by an agreement, except as provided by certain listed statutes. States that a general provision to excuse liability or limit remedies won't work to change the obligations imposed by this chapter.

AS 45.05.103(d). States that the rights and obligations of an issuer to a beneficiary, or to a nominated person, are independent of the contracts and arrangements underlying the letter of credit. In other words, the existence, performance, and nonperformance of the underlying contract or arrangement don't affect the rights and obligations under the letter of credit.

Includes under this subsection contracts between the issuer and the applicant and between the applicant and the beneficiary.

**Section 6.** AS 45.05.104. Sets out just what a letter of credit and certain related documents must consist of. They must be in a form that can provide a record and must be authenticated by a signature or authenticated as required under the parties' agreement or by the standard practice referred to in AS 45.05.108(e).

**Section 7.** AS 45.05.105. States that you don't need consideration (something of value to be received by a party) in order to issue, amend, transfer, or cancel a letter of credit, advice, or confirmation. Contracts usually require that each party receive something as consideration (not necessarily money or other property, but something of value to the party).

**Section 8.** AS 45.05.106(a). States that a letter of credit becomes enforceable against the issuer when the issuer sends it to the beneficiary or adviser. States that you can't revoke a letter of credit unless the letter says so.

AS 45.05.106(b). States that an amendment or cancellation of a letter of credit does not affect the rights and obligations of certain listed persons (e.g., beneficiary and applicant) unless they consent to the amendment or cancellation, or unless the letter of credit says it is revocable or that the issuer can amend or cancel it without the consent.

AS 45.05.106(c). States when a letter of credit expires if it does not state the date or does not have a provision that determines when it expires. The letter of credit expires one year after its stated date of issuance or, if not stated, one year after the date it is issued.

AS 45.05.106(d). States that a perpetual letter of credit expires five years after its stated date of issuance or, if not stated, five years after the date it is issued.

**Section 9.** AS 45.05.107(a). States that a confirmer is directly obligated on the letter of credit and has the rights and obligations of the issuer (as far as the letter of confirmation says it does). Also states that the confirmer has rights against, and obligations to, the issuer as if the issuer were the applicant and the confirmer had issued the letter of credit at the request of the issuer.

AS 45.05.107(b). States that a nominated person does not have to honor or give value when the necessary documents are presented to collect under a letter of credit, unless the person is also a confirmer.

AS 45.05.107(c). States that a person requested to advise may decline to act as an adviser. States that an adviser is not required to honor or give value when the necessary documents are presented to collect under a letter of credit, unless the adviser is also a confirmer. States that an adviser's job is to advise accurately about the terms of the letter of credit and related

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documents, and, with regard to the beneficiary, to check if the request to advise is authentic. States that a letter of credit, confirmation, or amendment is enforceable as issued even if the advice is not accurate.

AS 45.05.107(d). States that a person who notifies a transferee beneficiary (a person to whom the beneficiary has transferred the beneficiary's interest under the letter of credit) about the terms of a letter of credit or related document has the rights and obligations of an adviser under (c) of this section. States that the terms of the notice to the transferee beneficiary and transferor beneficiary (the beneficiary who transferred the interest in the letter of credit) may be different, as allowed by the letter of credit or related document that is received by the person who notifies the transferee beneficiary.

**Section 10.** AS 45.05.108(a). Except as provided in the section on fraud and forgery, requires an issuer to honor a presentation that appears on its face to comply strictly with the letter of credit. The standard practice of financial institutions determines whether the presentation complies as required. Requires an issuer to dishonor a presentation that does not appear to comply, except as provided in AS 45.05.113 or otherwise agreed with the applicant.

AS 45.05.108(b). States that upon presentation an issuer has a reasonable time to perform certain acts. The reasonable time may not exceed seven business days after the day of receipt. These acts are to honor the presentation, to notify the presenter that there are problems, or, if the letter of credit provides for honor after seven business days after presentation, to accept a draft (check) or incur a deferred obligation.

AS 45.05.108(c). States that in two situations an issuer is prevented from asserting that a problem causes the issuer to dishonor the letter of credit. The first situation is when the issuer does not give timely notice of the problem. The second situation is if the issuer gives notice but the problem is not stated in the notice. This subsection is subject to the fraud, forgery, and expiration assertions under (d).

AS 45.05.108(d). States that an issuer can still assert that there has been fraud or forgery (under AS 45.05.109(a)) or that the letter of credit has expired before presentation in order to dishonor a presentation, even if the issuer failed to give the required notice or to mention the fraud, forgery, or expiration in the notice.

AS 45.05.108(e). Requires an issuer of a letter of credit to comply with the standard practice of financial institutions that regularly issue letters of credit when the issuer handles letters of credit. States that a court is the determiner of whether the issuer has complied with the standard practice. Directs a court to allow the parties to present evidence of what is the standard practice.

AS 45.05.108(f). States what an issuer is not responsible for. An issuer is not responsible for the performance or nonperformance of the contract, arrangement, or transaction underlying the letter of credit. An issuer is not responsible for another person's acts or omissions. An issuer is not responsible for knowing the usage of a particular trade, except for the standard practice of financial institutions issuing letters of credit.

AS 45.05.108(g). Directs an issuer to ignore certain nondocumentary conditions contained in a letter of credit.

AS 45.05.108(h). Requires an issuer who does not honor a presentation under a letter of credit to return the documents presented, or to hold them for the presenter and notify the presenter.

AS 45.05.108(i). Establishes certain rights and limitations for an issuer when the issuer honors a presentation under a letter of credit. The issuer is entitled to be reimbursed by the applicant; the reimbursement must be made in funds that are available immediately to the issuer not later than the date of payment. The issuer takes the documents presented without any claims by the beneficiary or presenter. The issuer may not claim a right of recourse under AS 45.03.414 - 45.03.415 on a draft (check). Except as provided in two other sections, the issuer may not get the money or another valuable back if there was a mistake, if the mistake involves obvious problems in the documents or tender that are apparent on the face of the presentation. The issuer is discharged unless a required signature of the beneficiary was forged.

**Section 11.** AS 45.05.109(a). Gives an issuer directions on what to do if presentation documents appear to meet the requirements of the letter of credit, but a document is either forged or materially fraudulent, and honoring the documents would result in a material fraud by the beneficiary on the issuer or applicant.

Directs the issuer to honor the presentation of the documents if honor is demanded by certain persons under certain circumstances. The first is a nominated person that has given value in good faith and without notice of the forgery or fraud. The second is a confirmor that has honored its confirmation in good faith. The third is a holder in due course of a draft (check) that was drawn up under the letter of credit and taken by the holder in due course after acceptance by the issuer or nominated person. The fourth is the person who has had the issuer's or nominated person's deferred (doesn't have to be paid immediately) obligation transferred (assigned) to the person, if before the obligation was incurred by the issuer or nominated person, the person gave value to get the assignment and did not have notice of the forgery or fraud.

Allows the issuer to honor or dishonor the request for payment if the issuer acts in good faith and if the situation does not fall under categories (1) - (4) above.

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AS 45.05.109(b). Authorizes a court to enjoin an issuer from honoring a request for payment (or grant similar relief against the issuer or other persons) when an applicant claims forgery or fraud, but only if four listed conditions are met. The first is that the relief must not be prohibited under the law governing drafts that have been accepted by the issuer, or governing a deferred obligation incurred by the issuer. The second is that a beneficiary, issuer, or nominated person who may be adversely affected must be adequately protected against loss resulting from the court giving the relief. The third is that all of the conditions for obtaining the court relief in this state must be satisfied. The fourth is that applicant is likely to succeed on the claim of forgery or fraud and the person demanding that the presentation be honored does not qualify for protection under (a)(1)

**Section 12.** AS 45.05.110(a). Establishes certain things that the beneficiary warrants when the presentation is honored. The beneficiary warrants to the issuer, to another person to whom the presentation is made, and to the applicant that there is no fraud or forgery as those terms are described in AS 45.05.109(a). The beneficiary warrants to the applicant that the payment (or transfer of value) does not violate an agreement between the beneficiary and the applicant or another agreement connected to the letter of credit.

AS 45.05.110(b). States that the warranties in (a) are in addition to other warranties under AS 45.03 (UCC: negotiable instruments), AS 45.04 (UCC: bank deposits and collections), AS 45.07 (UCC: warehouse receipts, bills of lading, and other documents of title), and AS 45.08 (UCC: investment securities) that are related to the presentation or transfer of the documents.

**Section 13.** AS 45.05.111(a). Allows a beneficiary, successor beneficiary, or a nominated person to recover from the issuer of a letter of credit the amount in dispute if the issuer wrongfully dishonors or states that the issuer will not honor its obligation. If the issuer's obligation is not to pay money, this subsection allows the claimant to make the issuer perform what the issuer was supposed to perform, or, if the claimant elects, to recover an amount of money that equals the value of the performance. Allows the claimant to also recover damages that flow directly and immediately from the dishonor but not more remote damages. States that the claimant does not have to take action to avoid the damages that might result. However, reduces the awarded damages to the extent the claimant does avoid the damages. Requires the issuer to prove the amount of the damages that the claimant avoided. If the claim is based on the issuer repudiating the obligation before presentation of the documents, states that the claimant does not have to present the documents normally required to require the issuer to pay or deliver the value required.

AS 45.05.111(b). Allows the applicant to recover damages from the issuer if the issuer wrongfully dishonors a draft or demand presented under a letter of credit, or if the issuer wrongfully honors a draft or demand under the letter of credit. Allows the claimant to recover damages that flow directly and immediately from the wrongful act, but not the more

remote "consequential" damages. Reduces the amount of awarded damages by any amount saved due to the wrongful act.

AS 45.05.111(c). Allows a person to recover from an adviser or nominated person, other than a confirmer, the person's damages resulting from the adviser's or nominated person's breach of an obligation under this chapter or from an issuer's breach of an obligation not covered by (a) or (b). Allows the person to recover only damages that flow directly and immediately from the breach, but not the more remote consequential damages, less any amount the person saves due to the breach. States that a confirmer has the liability of an issuer under (a), (b), and this subsection, to the extent of the confirmation.

AS 45.05.111(d). States that an issuer, a nominated person, or an adviser who is liable under (a) - (c) must pay interest on the amount owed from the date of the wrongful dishonor, or from another appropriate date.

AS 45.05.111(e). Directs the court to award attorney fees and costs to the party who wins a court action for a remedy under this chapter.

AS 45.05.111(f). Allows parties to establish ahead of time by agreement the amount of damages that would result from a breach of an obligation under this chapter. However, the amount or formula for calculating the amount must be reasonable.

**Section 14.** AS 45.05.112(a). Prohibits transferring the right of a beneficiary to payment or performance under a letter of credit, except when the transfer occurs by operation of law as provided under AS 45.05.113, or unless the letter of credit says the right is transferable.

AS 45.05.112(b). Allows in two circumstances an issuer to refuse to carry out or recognize a transfer, even if allowed under the letter of credit. The first circumstance is that the transfer would violate the law that applies to the situation. The second circumstance is that the transferor or the transferee has failed to comply with the letter of credit, or with another requirement that relates to the transfer, and that is within the standard practice of financial institutions regularly dealing with letters of credit or that is otherwise reasonable under the circumstances.

**Section 15.** AS 45.05.113(a). Allows a person who succeeds another person as the beneficiary under a letter of credit to perform certain listed acts without having to disclose that it is a successor of the beneficiary. The successor may consent to amendments. The successor may sign and present documents. The successor may receive payment or other items of value in the name of the beneficiary.

AS 45.05.113(b). Allows the successor of a beneficiary to perform certain listed acts in its own name as the disclosed successor to the beneficiary. The disclosed successor may consent to amendments. The disclosed successor may sign and present documents. The

disclosed successor may receive payment or other items of value. Except as provided by (e), directs an issuer to recognize a person who is disclosed to be a successor beneficiary as a full beneficiary if the successor beneficiary complies with the standard practice for financial institutions regularly dealing in letters of credit, or, in the absence of the standard practice, with other reasonable procedures that will protect the issuer.

AS 45.05.113(c). States that an issuer does not need to determine whether a person alleging to be a successor beneficiary is actually such a beneficiary or whether the purported successor's signature is genuine or authorized.

AS 45.05.113(d) States that honoring a purported successor's presentation under (a) or (b) that appears to be in compliance has the consequences identified in AS 45.05.108(i) even if the person is not really the successor of the beneficiary. States that documents signed in the name of the beneficiary or a disclosed successor by a person who is not really the beneficiary or the successor beneficiary are considered to be forged documents when applying AS 45.05.109.

AS 45.05.113(e). Allows an issuer (if the issuer's rights of reimbursement are not covered by (d) or by similar law), any confirmer, and any nominated person to decline a presentation as provided in (b).

AS 45.05.113(f). States that if a beneficiary changes its name after a letter of credit is issued, the beneficiary has the same rights and obligations as a successor beneficiary under this section.

**Section 16.** AS 45.05.114(a) Allows a beneficiary to assign (transfer to another person) its right to the proceeds of a letter of credit. Allows the beneficiary to do this before presentation, by assigning the right to receive proceeds when the conditions are satisfied in the letter of credit.

AS 45.05.114(b). Allows the issuer or nominated person to refuse to recognize an assignment of the proceeds of a letter of credit until the issuer or nominated person agrees to the assignment.

AS 45.05.114(c). States that an issuer or nominated person is not required to give or withhold its consent to an assignment (transfer to another person) of the proceeds of a letter of credit. Prohibits the issuer or nominated person from withholding the consent unreasonably if the assignee has and shows the letter of credit and if presentation of the letter of credit is required before honor.

AS 45.05.114(d). States that the rights of a transferee beneficiary (a subsequent beneficiary to whom a beneficiary's rights have been transferred) or of a nominated person do not depend

on the beneficiary's assignment (transfer) of the proceeds of a letter of credit and are superior to the assignee's right to the proceeds.

AS 45.05.114(e). States that the rights under this section between an assignee and an issuer, a transferee beneficiary, or a nominated person, and the issuer's or nominated person's payment of proceeds to an assignee or a third person, do not affect the rights between the assignee and a person other than the issuer, transferee beneficiary, or nominated person. States that the creation and perfecting (making effective) of a security interest (an interest taken to secure a payment) in (or granting) a beneficiary's rights to proceeds, and assignment of (transferring) those rights, are governed by AS 45.09 (UCC: secured transactions) or other law. States that the rights and obligations arising on the creation and perfection of a security interest or arising on another assignment (transfer) of a beneficiary's rights to proceeds, are governed by AS 45.09 or other law, as against a person other than the issuer, transferee beneficiary, or nominated person.

AS 45.05.114(f). Defines "proceeds of a letter of credit" for the section.

**Section 17.** AS 45.05.115. Limits how long a person has to bring an action in court to enforce a right or obligation under this chapter. Limits the time to the later of (1) one year after the expiration date of the letter of credit, or (2) one year after the basis for the action occurs. States that a basis for the action arises when there is a breach (of an obligation) under this chapter, even if the injured party does not know about the breach.

**Section 18.** AS 45.05.116(a). States that the liability of an issuer, a nominated person, or an adviser is governed by the jurisdiction that the parties choose by agreement if the agreement is in the form of a record signed or otherwise shown to be authentic by the parties under AS 45.05.104 or by a provision in the letter of credit, confirmation, or other undertaking. States that the selected jurisdiction is not required to be related to the transaction involved.

AS 45.05.116(b). States which jurisdiction governs the liability of certain listed persons for their acts or failure to act, unless (a) applies. States that the jurisdiction is the jurisdiction where the person is located. Considers the person to be located at the address stated in the person's promise. States that if more than one address is indicated, the person is considered to be located at the address from which the promise of the person was issued. When dealing with jurisdiction, selection of whose law to apply, and recognition of letters of credit between bank branches, but not a court judgment, the branches of a bank are considered to be separate judicial entities, and a bank is considered to be located where the bank's branch that is related to the matter is considered to be located under this subsection.

AS 45.05.116(c). States that, except as provided otherwise in this subsection, the liability of certain listed persons is governed by rules of custom or practice that the parties expressly select for the letter of credit or confirmation, or undertaking. Gives as an example the

Uniform Customs and Practice for Documentary Credits. States that if both this chapter and the rules of custom or practice apply to the liability, the rules govern, unless they conflict with a provision of this chapter that cannot be changed (see AS 45.05.103(c)).

AS 45.05.116(d). States that this chapter governs if a conflict occurs between this chapter and AS 45.03 (UCC: negotiable instruments), AS 45.04 (UCC: bank deposits and collections), AS 45.09 (UCC: secured transactions), and AS 45.14 (UCC: funds transfers).

AS 45.05.116(e). States that the location for settling disputes under this chapter may be chosen in the same manner as the governing law is chosen under (a), and that the selection has the same binding effect.

**Section 19.** AS 45.05.117(a). States that an issuer who honors a letter of credit is subrogated to the rights of (is substituted for and can claim the rights of) certain listed persons. The first person is the beneficiary, and the substitution is the same as if the issuer were a back-up debtor on the underlying obligation owed to the beneficiary. The second person is the person who requested the issuer to issue a letter of credit and the subrogation is to the same extent as if the issuer were the back-up debtor on the obligation owed to the applicant.

AS 45.05.117(b). States that an applicant that reimburses an issuer is subrogated to the rights of (is substituted for and can claim the rights of) certain listed persons. The subrogation is to the same extent as if the applicant were the secondary debtor on the obligation owed to the issuer, and the applicant has the subrogation rights of the issuer to the rights of the beneficiary stated in (a).

AS 45.05.117(c). States that a nominated person who pays or gives value against a draft (check) or demand presented under a letter of credit is subrogated to the rights of (is substituted for and can claim the rights of) certain listed parties.

AS 45.05.117(d). States that the right of subrogation in (a) and (b) don't arise until the issuer honors the letter of credit or otherwise pays under the letter of credit. States that the rights of subrogation in (c) don't arise until the nominated person pays or otherwise gives value under the letter of credit. These provisions apply even if there is an agreement that states otherwise. Until the events occur, the persons do not obtain under this section any present or future rights that would form the basis for a claim, defense, or excuse.

**Section 20.** AS 45.09.103(a). This amendment adds "rights to proceeds of written letters of credit" to the items that are covered by this section. The section deals with determining which jurisdiction's law applies when perfecting (making effective) secured transactions (agreements where one party transfers an interest in property to secure a contract).

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**Section 21.** AS 45.09.104. States that AS 45.09 (UCC: secured transactions) does not apply to the transfer of an interest in a letter of credit, except for the rights to proceeds of a written letter of credit.

**Section 22.** AS 45.09.105(c). Adds two definitions to the definitions that apply in AS 45.09 (UCC: secured transactions): "letter of credit" and "proceeds of a letter of credit."

**Section 23.** AS 45.09.106. Adds "rights to proceeds of written letters of credit" to the definition of "general intangibles" that is used in AS 45.09 (UCC: secured transactions).

**Section 24.** AS 45.09.304(a). States that to perfect (make effective) a security interest (interest given to a person to secure performance of a contract) in the rights to proceeds of a written letter of credit, the party that is secured must take possession of the letter of credit.

**Section 25.** AS 45.09.305. Allows a person to obtain an interest that secures performance of an obligation in the "rights to proceeds of a written letter of credit" by taking possession of the letter of credit.

**Section 26.** Subsection (a) states that this Act applies to a letter of credit that is issued on or after the effective date of this Act. States that this Act does not apply to a transaction, event, obligation, or duty that is associated with a letter of credit issued before the effective date of this Act.

Subsection (b) states that a transaction associated with a letter of credit issued before the effective date of this Act, and the accompanying rights, obligations, and interests are governed by current law as if this Act had not occurred.

**Section 27.** Makes the Act effective January 1, 1998.

TLB:jdr

97-174.jdr

# STATE OF ALASKA

## DEPARTMENT OF LAW

### OFFICE OF THE ATTORNEY GENERAL

April 29, 1997

The Honorable Norman Rokeberg  
House Labor and Commerce Committee Chair  
State of Alaska  
State Capitol  
Room 110  
Mailstop 3100  
Juneau, AK 99801-1182

Re: HB 178 - An Act relating to  
Letters of Credit  
Our file: 661-97-0626

Dear Representative Rokeberg:

Pursuant to your request at the committee hearing on Friday afternoon, April 25, 1997, I would offer the following comment on the timing provisions of proposed AS 45.05.103.

Under the existing Uniform Commercial Code - Letters of Credit an issuer may defer honoring a letter of credit until the close of the third banking day following receipt of the documents and may further defer honoring if there is implied consent. Dishonor occurs if the issuer fails to honor within the prescribed period. AS 45.05.112(a) and (b). There is no requirement that the issuer give notice to the beneficiary of reasons for dishonoring the letter of credit.

Under the proposed AS 45.05.108(b) an issuer is given a reasonable time after presentation, but not more than seven days after presentation, in which to honor or give notice of any discrepancies. The key change is that the issuer is expressly precluded from later asserting any discrepancies not timely specified (except for fraud, forgery, or expiration).

The Official Comment provided by The American Law Institute and the National Conference of Commissioners on Uniform State Laws, dated November 13, 1995, notes that the time within which the issuer must honor or give notice of discrepancies is the

APR 30 1997

TONY KNOWLES, GOVERNOR

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Representative Norman Rokeberg  
Our File: 661-97-0626

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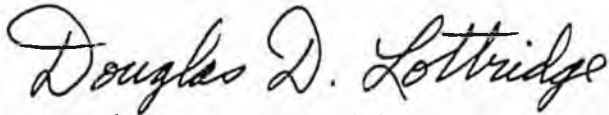
lessor of a reasonable amount of time or seven business days. For instance it would be unreasonable for an issuer to determine on the first day that it will not honor the presentation and then wait until the seventh day to notify the presenter, thus depriving the presenter of time in which to cure the discrepancies. This would be especially true if the letter of credit were about to expire.

The commentary further stresses that the section is designed to balance the need of the issuer to have time to examine the documents against the possibility that the examiner will take excessive time to search for defects. Although under the proposed law the issuer may in some circumstances have additional time to dishonor a presentation, the intended balance is that the reasons must be specified or waived. This provision also gives the beneficiary a more timely opportunity to cure any defects.

In order to assist your committee's further consideration of the bill and proposed amendments I am attaching a copy of a memorandum to Art Peterson and Deborah Behr from John McCabe, the Legislative Director/Legal Counsel of the National Conference of Commissioners on Uniform State Laws. Prior to receiving a copy of John McCabe's memorandum, Jerry Kurtz and I had independently reached conclusions similar to those expressed by Mr. McCabe.

Sincerely,

BRUCE M. BOTELHO  
ATTORNEY GENERAL

By:   
Douglas D. Lottridge  
Assistant Attorney General

DDL:fgf

cc: Pat Pourchot  
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February 20, 1996

The Honorable Pete Kott, Chair  
House Labor and Commerce Committee  
Alaska State Legislature  
Room 432, State Capitol  
Juneau, AK 99801-1182

**HAND-DELIVERED**

Re: Uniform Commercial Code, Revision of Article 5  
(Letters of Credit)

Dear Representative Kott:

As I discussed briefly with your assistant, George Dozier, on February 16, 1996, you'll find attached an information packet on the revision of Article 5 of the Uniform Commercial Code (UCC). This revision was promulgated by the National Conference of Commissioners on Uniform State Laws (NCCUSL), the same body that produced the entire UCC a few decades ago.

The basic purpose of this revision is to update the law governing the \$200 billion U.S. letter-of-credit industry. All 50 states and Puerto Rico, Guam, and the District of Columbia have adopted the UCC, including Article 5. It is now necessary for Article 5 to be revised, to recognize changes in technology and in commercial practices, so as to avoid litigation over the increasing number of issues that are no longer adequately dealt with in the decades-old current law. One of the main features of this revision is the simplification of Article 5. Another is its recognition of Uniform Customs and Practices for Documentary Credits, a body of material that is used in connection with most international letters of credit.

I would be happy to provide any additional information that you may need. However, in Alaska's Uniform Laws delegation, Jerry Kurtz is the one with the most expertise in this area. He can be reached in Anchorage at 276-6100.

I hope that your committee will be able introduce this bill this session. I realize that introduction now might be too late for passage this session, but it is important to get this measure into the public eye as soon as possible, so that it can be studied. Then it can be reintroduced next legislature, for passage. Thank you for considering it.

Representative Pete Kott

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Yours truly,



Arthur H. Peterson  
Uniform Law Commissioner for Alaska

Enclosure

cc w/o enc.: Rest of Alaska's ULC Delegation:  
Honorable Jay A. Rabinowitz  
W. Grant Callow, Esq.  
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L. S. Kurtz, Jr., Esq.  
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**ALASKA STATE LEGISLATURE**  
**House of Representatives**

COMMITTEE ASSIGNMENTS:

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**Representative Norman Rokeberg**

MEMORANDUM

DATE: February 18, 1997

TO: Terry Bannister, Attorney  
Legal Services  
Legislative Affairs Agency

FROM: Representative Rokeberg 

RE: UCC Article 5 - Draft Legislation

Enclosed are letters from Arthur Peterson, Esq. of February 20, 1996, and September 26, 1996, and Mr. L. S. Kurtz, Jr., Esq. of October 3, 1996, and October 4, 1996, as well as other memorandums of interest regarding UCC Article 5, Letters of Credit revisions to HB 553 of the 19th Legislature which was introduced by the House Labor & Commerce Committee.

I understand you have had conversations with Mr. Peterson regarding this potential bill. If you would be so kind as to create a draft for new legislation to be introduced by the House Labor and Commerce Committee by request, I would appreciate it.

MAR 05 1997

## LEGAL SERVICES

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Juneau, Alaska 99801-2105

### MEMORANDUM

April 10, 1996

**SUBJECT:** Bill draft on letters of credit under the Uniform Commercial Code  
(Work Order No. 9-LS1794\A)

**TO:** Representative Pete Kott, Chair  
House Labor and Commerce Committee  
Attn: George Dozier

**FROM:** Theresa Bannister  
Legislative Counsel

This memo accompanies the draft described above.

I have revised the submitted material as necessary to put it in the legislature's drafting style. You are welcome to review the mark-ups I made while drafting the material you submitted.

The following changes, comments, and questions are provided for your review. Since some of the changes required interpretation of intent, you may want to have them reviewed for accuracy by a representative of the National Conference of Commissioners on Uniform State Laws (NCCUSL) or by another person familiar with the requested revision.

1. AS 45.02.512(a)(2). Because the language of AS 45.02.512(a)(2) is slightly different from the current uniform language, the requested amendments were made to AS 45.02512(a)(2) as it exists now in our statutes; I did not try to make the amended language conform completely to the current uniform language.
2. AS 45.05.102. In (a)(3), "the letter of credit's" is used instead of "its." In (a)(5), I used "the timely failure" instead of "failure timely." In (a)(6), "standard practices" is used instead of "standard practice," and "and that is not oral" is used instead of "a document may not be oral." In (b), the language is somewhat rewritten.
3. AS 45.05.103(c). It is not clear to me how definitions (AS 45.05.102(a)(9)-(10)) can be exceptions to the substance of the subsection.
4. AS 45.05.104(2). "Under" is used instead of "in accordance with," and "standard practices" is used instead of "standard practice."

5. AS 45.05.106. In (a), "provides that it is revocable" replaces "so provides." In (b), the second occurrence of "beneficiary, applicant, confirmer, or issuer" is used instead of "that person." In (c), "letter of credit" is used instead of "it," "letter of credit's" is used instead of "its," and "a date of issuance is not" is used instead of "none is." In (d), "letter of credit is" replaces "it is" at the end of the subsection, and "a date of issuance is not" replaces "none is."
6. AS 45.05.107. In (a), "confirmer's confirmation" replaces "its confirmation". In (c), used "to advise accurately as to the terms" instead of "accurately to advise the terms." "Received by the adviser" is used instead of "received by that person."
7. AS 45.05.107(d). "Who notifies the transferee beneficiary" is used instead of "who so notifies." "Terms in a notice" replaces "terms in any notice."
8. AS 45.05.108(a). "Standard practices" replaces "standard practice." At the end, "does not appear on its face to comply strictly with the terms and conditions of the letter of credit" is used instead of "does not appear so to comply."
9. AS 45.05.108. Replaced "its receipt" with "the issuer's receipt." In (b)(1), added "the presentation." In (c), the language is slightly rewritten.
10. AS 45.05.108. In (e) - (f), used "standard practices" instead of "standard practice." In (h), used "who dishonors" for "that has dishonored."
11. AS 45.05.108. Used "who honors" for "that has honored." In (i)(1), used "the payment of funds" instead of "its payment of funds." In (i)(5), used "the issuer's performance" instead of "its performance."
12. AS 45.05.109(a)(1). Changed to our standard present tense. Deleted "and" at the end of the paragraph because (1) and (2) cover different situations.
13. AS 45.05.109(a)(1)(B). Used "the confirmation" instead of "its confirmation."
14. AS 45.05.109(a)(1)(C). Used "and that is taken" instead of "which was taken."
15. AS 45.05.109(a)(1)(D). Added "if the obligation" after the first "obligation."
16. AS 45.05.109(a)(2). Used "in a case not covered by (1) of this subsection" instead of "in any other case."
17. AS 45.05.109(b). Rewritten to avoid using the ambiguous "only."

Representative Pete Kott  
April 10, 1996  
Page 3

18. AS 45.05.109(b)(2)-(3). In (2) used "the beneficiary, issuer, or nominated person" instead of "it" before "may suffer." In (3) used "are met" instead of "have been met." In (3), used "that entitle" instead of "to entitle."
19. AS 45.05.110(a). Used "if a presentation" instead of "if its presentation."
20. AS 45.05.111(a). In the third to the last sentence, used "is reduced" instead of "must be reduced." In the last sentence used "does not need to present a document" instead of "need not present any document."
21. AS 45.05.111(b). Used "the issuer's" instead of "its."
22. AS 45.05.111(d)-(e). Used "owed under the liability" instead of "owed thereunder." Current court rule already allows attorney fees to the prevailing party and establishes how to calculate them. In (e) "reasonable" attorney fees are allowed; this is a different standard than the court rule.
23. AS 45.05.112(b)(2). Rewrote the paragraph slightly to make it clear that (A) and (B) modify "another requirement." Used "standard practices" instead of "standard practice."
24. AS 45.05.113(b). Used "the successor's predecessor" instead of "its predecessor." In the second sentence, used "if there is compliance with" instead of "upon compliance with" to make the language clearer; it was not clear just what "upon" meant (e.g. when there is compliance, or if there is compliance). In (b)(2) used "of the standard practices under AS 45.05.108(e)" instead of "of such a practice, compliance with"; please examine to see if acceptable.
25. AS 45.05.114. The subsection containing the definition of "proceeds of a letter of credit" was placed at the end of the section as subsection (f).
26. AS 45.05.114(a). Rewrote the second sentence to make it clearer.
27. AS 45.05.114(b). Used "the issuer or nominated person consents" instead of "it consents."
28. AS 45.05.114(c). Replaced "has no" with "does not have an." Added "if" before "presentation."
29. AS 45.05.114(e). In the last sentence, used "as against" instead of "against." Added "and perfection" after "the creation" and deleted "and its perfection" later on in the sentence. Changed "right to proceeds" to "rights to proceeds."

Representative Pete Kott

April 10, 1996

Page 4

30. AS 45.05.116(a)-(b). In (a) used "the letter of credit" instead of "the person's letter of credit." In (a), used "does not need to bear a" instead of "need not bear any." In (b), replaced "person" with "issuer, nominated person, or adviser" throughout the subsection. In (b), "the bank's relevant branch" replaces "its relevant branch."

31. AS 45.05.116(c). It would be helpful to insert more information on the "Uniform Customs and Practice for Documentary Credits" (e.g. who establishes, what version to use).

32. AS 45.05.117. In (a), the provisions are broken out according to my understanding of them. In (b), used "to the issuer, and the applicant has" instead of "to the issuer and has."

33. AS 45.05.117(d). Added a comma after "otherwise pays" to make the subsection clearer under my understanding of the subsection.

34. AS 45.09.106. The section does not contain the reference to "investment property" found in the submitted material, because the submitted material reflects the section after a revision of AS 45.08 (investment securities), and the revision has not been made in this state.

35. In AS 43.09.305, changed "right to proceeds" to "rights to proceeds."

36. I added a delayed effective date so that affected persons have an opportunity to prepare for the changes. Is this what you want? If so, is the date appropriate?

If I may be of further assistance, please advise.

TLB:klb

96-205.klb

Enclosure

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TAX ID NO. 92-0037399

October 4, 1996

Arthur H. Peterson, Esq.  
Dillon & Findley  
350 N. Franklin Street  
Juneau, AK 99801

Dear Art:

RE: Uniform Commercial Code Revised Article 5 -  
Letters of Credit - Memorandum from Theresa Bannister  
dated April 10, 1996

It is seldom that I question Alaska's redrafting of legalese into understandable English, but I fear we may be going too far with Article 5. I will leave it up to your judgment whether to pass this opinion onto Theresa Bannister or Representative Pete Rott. Referenced by corresponding paragraphs of Theresa's April 10 memo, here are the concerns I have which I consider serious enough to warrant amendment of the pending bill:

2. In (a) (5) "timely" is intended to modify "honor" and "take" rather than "failure". Theresa's change makes it modify only "failure", which isn't the object. In (a)(6) and all other places where it appears "standard practice" should be retained rather than replaced by "standard practices". I hate to think about how an Alaska court might tackle this change from the NCCUSL version. The NCCUSL version in describing "standard practice" in Section 5-108 painstakingly tells the court in subsection (e) to determine one standard practice. Our proposed version leaves it open to the court to find several standard practices. In the real world different issuers will observe different practices, and different financial institutions will even observe different practices. It is critical that we join other states adopting this legislation in requiring that the court find one standard practice (which I admit will be a conglomeration of varying practices). This is particularly important in Alaska, where it is hard to find any two banks handling anything exactly the same way, and where there may be few financial institutions "that regularly issue letters of credit."

8. The NCCUSL wording tells me that "does not appear so to comply" requires any issuer to desire "a presentation that, as determined by the

Arthur H. Peterson, Esq.  
October 4, 1996  
Page 2

standard practice referred to in Subsection (e), appears on its face strictly to comply with the terms and conditions of the letter of credit." Theresa's change could lead a court to ignore the underscored language when interpreting the second sentence of section (a). If her changes do stand, it should include all of the underscored language.

10. "Who" or "that"? Neither one is correct, because an issuer may be an "it", a "him" or a "her." Theresa obviously decided to use "that." as an expedient solution to this dilemma. Why should we use a different expedient solution and causes judges to ponder why we did it?

11. Same problem as 10. Same comments here and wherever else change is made.

12. As you point out, "and" is still necessary.

13. Dangerous change because there may be more than one confirmer. Only the confirmer who has honored its confirmation in good faith should be able to take advantage of clause (ii) which is our clause (B).

17. I agree with you that "only" does not create an ambiguity. However, our section may. If we are going to retain it, I believe "not" at the end of line 6 should be replaced with "neither" and "or" at the end of line 7 should be replaced with "nor".

19. There could be more than one presentation. Our change is ill-advised because the beneficiary should warrant nothing unless its presentation is the one honored.

22. I agree with your thought that we should refer to the Civil Rules.

24. I agree with your comment.

26. I can't decide whether the NCCUSL version or Theresa's version is more clear. In such situations, I think we should stick with NCCUSL. I would write it more like this: "An assignment by the beneficiary prior to presentation is a present assignment of the beneficiary's right to receive proceeds contingent upon the beneficiary's compliance with the terms and

Arthur H. Peterson, Esq.  
October 4, 1996  
Page 3

conditions of the letter of credit. (That may be a further reason to stick with the NCCUSL version!)

29. Moving "into perfection" is extremely dangerous. The concept of perfection is used outside of UCC Article 9, but this could be construed to limit the application of perfection to a security interest. If there is any chance of that, perfection would be kept where NCCUSL puts it.

30. "Judicial" is misspelled in line 4 of page 14.

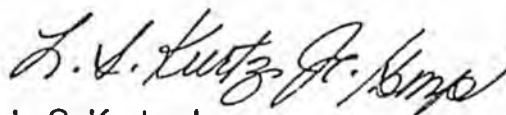
31. I agree with your comment, but believe we should not touch this. In the future we may have several sets of uniform customs and practice, but we want to leave room open to let the court's decide which version is applicable on any given page.

33. The comma helps, but it would be safer if we make any change to add "of subrogation stated in subsection" ahead of (c). Without that additional change, I would rather stick with the NCCUSL version for purposes of uniformity. Uniformity is particularly critical in this area of the law. When has anyone seen an Alaska case concerning letters of credit? We will be relying upon other states for case law in this area for the foreseeable future.

An overriding reality in dealing with Article 5 in Alaska is that we probably do not have an attorney in the state expert in letter of credit matters. I have dealt with miscellaneous letter of credit problems here and there, as have other bank attorneys, but the people that put together this revision of Article 5 are so far ahead of any talent we can apply to the subject that we should be extremely cautious about changing what they have done. That fact plus the low probability of us accumulating any case law makes caution a good watch word.

Sincerely,

BURR, PEASE & KURTZ



L. S. Kurtz, Jr.

BURR, PEASE & KURTZ

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TAX ID NO. 92-0037399

October 3, 1996

Ms. Shirley Worthy  
National Conference of Commissioners  
on Uniform State Laws  
676 North St. Clair Street, Suite 1700  
Chicago, IL 60611

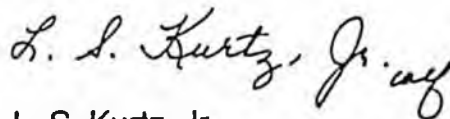
Dear Shirley:

RE: Uniform Commercial Code Revised Article 5 -  
Letters of Credit

Please send me whatever information you have on how many states now have adopted Revised Article 5. We obtained introduction of this article in our Legislature last spring and hope to obtain enactment of it in the 1997 session, which commences in January. Any information you have indicating additional states which are about to adopt Revised Article 5 also would be most helpful.

Sincerely,

BURR, PEASE & KURTZ



L. S. Kurtz, Jr.

✓ cc:

Arthur Peterson, Esq.  
Dillon & Findley, Juneau  
350 N. Franklin St.  
Juneau, AK 99801

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Hon. Pete Kott, Chair  
House Labor & Commerce Committee  
Alaska State Legislature  
10928 Eagle River Rd., Suite 1441  
Eagle River, Alaska 99577

Re: HB 553, Uniform Commercial Code, Article 5  
(letters of credit)

Dear Pete:

As you requested, I have reviewed Legislative Counsel Terry Bannister's April 10, 1996 36-point memo to you, accompanying her draft of this UCC, art. 5 bill. As usual, she has done an excellent, meticulous job. My comments appear below.

When you and I last talked about this bill, last spring, you indicated that you planned to hold a committee hearing on it some time this fall, and I have been mentioning that idea to various people. What is the current status of that plan?

For the hearing, please be sure to notify Jerry Kurtz. You will recall that he is an Anchorage attorney who is one of our uniform law commissioners and is the one most experienced in this area of the law. His phone number is 276-6100.

Also, please be sure to notify John Tindall (278-8533), who is another Anchorage attorney and the chair of the Alaska Bar Association's Business Law Section, and John Beard (277-4531), an Anchorage attorney who does a lot of work with the Alaska Bankers' Association. Last spring, I sent Tindall one of the NCCUSL information packets I sent you, and his Business Law Section has been looking at it. I also sent one to Wes Coyner, the bankers' lobbyist, and I believe that he relayed it to Anchorage banker Jerry Weaver (who might have, in turn, relayed it to John Beard).

If you need another copy of that packet, you could call Katie Robinson, Legislative Assistant for the National Conference of Commissioners on Uniform State Laws, in Chicago. Her number is (312) 915-5962. (The general number for the NCCUSL is 915-0195.) Tell her that I suggested that you call her, and there should be no charge for the packet. (But the supply is limited.)

Now, on to the bill and Terry's memo:

HB 553 presents the NCCUSL's 1995 amendments to UCC, art. 5., including the one to sec. 5-111(e) (AS 45.05.111(e), at page 10 of the bill), which pertains to attorney fees and was distributed separately from the other amendments.

Although I have checked all 36 of Terry's points, and have looked at the bill generally, I have not made a line-by-line comparison of her version of the bill with the official NCCUSL version. It appears that HB 553 tracks the official version very carefully, with virtually identical wording, except as indicated in Terry's memo. Here are my responses to the items in that memo, using her item numbers:<sup>1</sup>

2. AS 45.05.102(a)(6). I think that Terry's change from "practice" to "practices" is o.k., assuming that there are several activities going on, and, thus, there are several practices. (NOTE that she has consistently made this change throughout the bill.) However, it is quite possible that, in the banking business, the singular "practice" is a term of art in this context, and we should leave the official version of the Act as is. Jerry Kurtz or John Beard or John Tindall could probably answer this question better than I.

3. AS 45.05.103(c). The referred-to definitions are listed to prevent them from being "varied" by agreement. The bill is o.k.

5. AS 45.05.107(a). I don't think that her change from "received by that person" to read "received by the adviser" is correct. The official version's "that person" is, indeed, ambiguous, but I don't think that "advice . . . received" "by the adviser" makes sense. I would suggest that Terry or Jerry Kurtz or your staff call John McCabe, Legal Counsel and Legislative Director for the NCCUSL (312-915-5976), for clarification.

12. AS 45.05.109(a)(1). Terry deleted the "and" between paragraphs (1) and (2). It should be restored, so that the subsection reads, quite properly, ". . . the issuer (1) shall . . . , and (2) may . . . . IN ADDITION, the second comma on page 8, line 22, added by Terry, should be deleted, so that the phrase reads "if honor is demanded by . . . ." AND I believe that the past perfect tense and the past tense should be restored, because the sense of the provisions is that the activity mentioned has

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<sup>1</sup> The items not listed here are o.k. While I might not have made all of the changes that Terry made in those places (such as the numerous changes of "it" or "its" to repeat the subject noun, and eliminating uses of the past and past perfect tenses), her changes are acceptable.

already occurred. On page 8, line 23, change "gives" to read "has given"; line 25, change "honors" to read "has honored"; lines 26, 27, 30, and 31, change "is" to read "was."

17. AS 45.05.109(b). I don't see the ambiguity in using "only" here, but the substance seems unchanged by Terry's re-wording.

19. AS 45.05.110(a). I believe that Terry's change to "if a presentation" should be returned to the official version's "if its presentation." The official version is, intentionally, more specific.

22. AS 45.05.111(d) and (e). Since Alaska is fairly unique in having a provision (Civil Rule 82) already providing for attorney fees being awarded to the winner in litigation, perhaps we should substitute a reference to Civil Rule 82 for the word "reasonable" in (e). And perhaps we should add a reference to Civil Rule 79 in (d). These changes would obviate the need for the bill's sec. 25 (and thus a separate vote on the floor), regarding changes in the court rules.

24. AS 45.05.113(b). I think that Terry's "if there is compliance with" should be returned to the official version's "upon compliance with." But I'm not sure it matters. However, in (b)(2), I believe that we need to restore the words "referred to in" in front of the reference to AS 45.05.108(e) because that subsection does not contain the practice[s]; it merely refers to the practice[s] of the financial institutions (the Uniform Customs and Practice [U<sup>C</sup>P]) discussed in the official version's prefatory note and mentioned in sec. 5-116(c) [proposed AS 45.05.116(c)].

31. AS 45.05.116(c). I agree with Terry that it would be helpful (even preferable) to provide more information about the U<sup>C</sup>P, but I don't have the answer. The reference is no mystery to the bankers and their lawyers, but other readers of this statute might benefit by greater specificity. It's not a major point, but perhaps John McCabe, or Connie Ring (chair of the NCCUSL drafting committee for these art. 5 amendments [703-448-2910]), could provide helpful language. If they can't, let it go.

34. AS 45.09.106. Terry was correct about the UCC art. 8 (investment securities) amendments at the time she wrote her memo. However, they have since been enacted -- ch. 17, SLA 1996 -- and page 17, line 7, of HB 553 should be amended by inserting the following after "instruments,": "investment property."

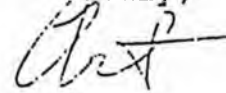
36. Section 27 of the bill should be changed for introduction next session to provide an effective date of July 1, 1997 or January 1, 1998. Terry's date was o.k. for the bill introduced last session.

Rep. Pete Kott  
HB 553 -- UCC art. 5 (letters of credit)  
September 26, 1996

Page 4

So, that's it. The bill looks good, and will be even a bit better with a couple of minor changes for its introduction next session. Thanks again for introducing it, and I hope you find this letter helpful. Good luck with and have fun at the hearing.

Yours truly,



Arthur H. Peterson  
Uniform Law Commissioner  
for Alaska

cc: Terry Bannister  
John Beard  
John Tindall  
L. S. (Jerry) Kurtz, Jr.

# ALASKA STATE LEGISLATURE

## House of Representatives

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## Labor and Commerce Committee

### MEMORANDUM

TO: Majority House Members

FROM: Representative Norman Rokeberg, Chairman  
House Labor & Commerce Committee

DATE: January 20, 1998

SUBJECT: HB 178 – Uniform Commercial Code: Letters of Credit

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HB 178 proposes to revise and bring up to date the Alaska Statutes in order to incorporate the changes in technology, language and commercial practices that have occurred since the original Uniform Commercial Code was enacted years ago.

L& C introduced the bill at the request of the National Conference of Commissioners based on revisions that they identified as necessary to avoid litigation. The proposed changes have been adopted by 50 other states and the District of Columbia.

HB 178 had three hearings and there was no testimony opposing the changes. The Alaska Bankers Association is on record as supporting this legislation.

I urge your support for this legislation.

# FISCAL NOTE

STATE OF ALASKA  
1998 LEGISLATIVE SESSION

BILL NO. HB 178

Revision Date: \_\_\_\_\_  
Title: UCC - Letters of Credit

Department: Commerce and Economic Development  
BRU: Banking, Securities and Corporations  
Component: Banking, Securities and Corporations

Sponsor: House Labor & Commerce  
Requestor: House Labor & Commerce

COMPONENT SERIAL NO. \_\_\_\_\_

Expenditures/Revenues

(Thousands of Dollars)

OPERATING EXPENDITURES	FY 99	FY 00	FY 01	FY 02	FY 03	FY 04
PERSONAL SERVICES						
TRAVEL						
CONTRACTUAL						
SUPPLIES						
EQUIPMENT						
LAND & STRUCTURES						
GRANTS, CLAIMS						
MISCELLANEOUS						
<b>TOTAL OPERATING</b>	0.0	0.0	0.0	0.0	0.0	0.0
<b>CAPITAL EXPENDITURES</b>	0.0	0.0	0.0	0.0	0.0	0.0
<b>CHANGE IN REVENUES</b>	0.0	0.0	0.0	0.0	0.0	0.0

FUND SOURCE

(Thousands of Dollars)

1002 Federal Receipts						
1003 GF Match						
1004 General Fund						
1005 GF Program Receipts						
1006 GF Mental Health						
Other						
<b>TOTAL</b>	0.0	0.0	0.0	0.0	0.0	0.0

Estimate of any current year (FY 98) cost: \$ 0.0

POSITIONS

FULL-TIME					
PART-TIME					
TEMPORARY					

ANALYSIS: (Attach a separate page if necessary)

Prepared by: Willis F. Kirkpatrick, Director  
Division: Banking, Securities and Corporations  
Approved by Commissioner: Debby Sedwick  
Agency: Commerce and Economic Development

Phone: 465-2521  
Date: 1-13-98  
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(7) . .  
Date Referred to Committee: March 6, 1997

FURTHER REFERRALS:

Date of Committee Action: 1/16/98

The LABOR AND COMMERCE Committee considered:

HB 178

HOUSE BILL NO. 178

UNIFORM COMMERCIAL CODE: LETTERS OF CREDIT

"An Act relating to letters of credit under the Uniform Commercial Code; and providing for an effective date."

recommends it be replaced with the following committee substitute \_\_\_\_\_ [ ] the same title  
[ ] a new title

[ ] additional referral to \_\_\_\_\_ Committee  
[ ] attached amendment(s)

ADOPTS: \_\_\_\_\_ Letter of Intent

ATTACHES NEW FISCAL NOTE(S): \_\_\_\_\_ (Dept)

APPROVES PREVIOUS: \_\_\_\_\_ (Dept/Date)

[ ] fiscal note(s) \_\_\_\_\_

[ ] fiscal note(s) \_\_\_\_\_

[X] zero fiscal note(s) DCED

[ ] zero fiscal note(s) \_\_\_\_\_

SIGNING WITH RECOMMENDATIONS	DP	DNP	NR	AM
<i>John Brudney</i>			✓	
<i>Tom Bick</i>			✓	
<i>Gene Ryan</i>			✓	
<i>John Rotelony</i>	✓			
<i>Gene Kishner</i>			✓	

CHAIR'S SIGNATURE

*[Handwritten Signature]*

1-16-98

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Copies of minutes listed below were originally included in this file. The minutes are available on the legislative computer database. In order to save space copies of minutes have not been left in the files.

Mary Pagenkopf

*House Labor & Commerce, March 14, 1997, 3:20 p.m.*

**HB**

**179**

# FISCAL NOTE

STATE OF ALASKA  
1997 LEGISLATIVE SESSION

BILL NO. CSHB 179 (L&C)

Revision Date: April 23, 1997  
 Title: An Act relating to fraternal societies; and providing for  
an effective date.  
 Sponsor: House L & C  
 Requestor: \_\_\_\_\_

Department: Commerce and Economic Development  
 BRU: Insurance  
 Component: Insurance  
 COMPONENT SERIAL NO. \_\_\_\_\_ 324

Expenditures/Revenues	(Thousands of Dollars)					
	FY 98	FY 99	FY 00	FY 01	FY 02	FY 03
<b>OPERATING EXPENDITURES</b>						
PERSONAL SERVICES						
TRAVEL						
CONTRACTUAL						
SUPPLIES						
EQUIPMENT						
LAND & STRUCTURES						
GRANTS, CLAIMS						
MISCELLANEOUS						
<b>TOTAL OPERATING</b>	<b>0.0</b>	<b>0.0</b>	<b>0.0</b>	<b>0.0</b>	<b>0.0</b>	<b>0.0</b>

<b>CAPITAL EXPENDITURES</b>						
-----------------------------	--	--	--	--	--	--

<b>CHANGE IN REVENUES</b>						
---------------------------	--	--	--	--	--	--

FUND SOURCE	(Thousands of Dollars)					
1002 Federal Receipts						
1003 GF Match						
1004 General Fund						
1005 GF/Program Receipts						
1006 GF/MHTIA						
Other						
<b>TOTAL</b>	<b>0.0</b>	<b>0.0</b>	<b>0.0</b>	<b>0.0</b>	<b>0.0</b>	<b>0.0</b>

Estimate of any current year (FY 97) cost: \$ 0.0

**POSITIONS**

FULL-TIME						
PART-TIME						
TEMPORARY						

**ANALYSIS:** (Attach a separate page if necessary)  
 This bill will not have a fiscal impact on the component.

Prepared by: Marianne K. Burke, Director  
 Division: Insurance  
 Approved by Commissioner: William L. Hensley  
 Agency: Commerce and Economic Development

Phone: 465-2515  
 Date: April 23, 1997  
 Date: 4-23-97

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# FISCAL NOTE

**STATE OF ALASKA**  
**1997 LEGISLATIVE SESSION**

**BILL NO. HB 179**

Revision Date: \_\_\_\_\_  
 Title: An Act relating to fraternal societies; and providing for  
an effective date.  
 Sponsor: House L & C  
 Requestor: \_\_\_\_\_

Department: Commerce and Economic Development  
 BRU: Insurance  
 Component: Insurance

COMPONENT SERIAL NO. \_\_\_\_\_ **324**

(Thousands of Dollars)

Expenditures/Revenues	FY 98	FY 99	FY 00	FY 01	FY 02	FY 03
<b>OPERATING EXPENDITURES</b>						
PERSONAL SERVICES						
TRAVEL						
CONTRACTUAL						
SUPPLIES						
EQUIPMENT						
LAND & STRUCTURES						
GRANTS, CLAIMS						
MISCELLANEOUS						
<b>TOTAL OPERATING</b>	0.0	0.0	0.0	0.0	0.0	0.0

<b>CAPITAL EXPENDITURES</b>						
-----------------------------	--	--	--	--	--	--

<b>CHANGE IN REVENUES</b>						
---------------------------	--	--	--	--	--	--

(Thousands of Dollars)

FUND SOURCE	FY 98	FY 99	FY 00	FY 01	FY 02	FY 03
1002 Federal Receipts						
1003 GF Match						
1004 General Fund						
1005 GF/Program Receipts						
1006 GF/MHTIA						
Other						
<b>TOTAL</b>	0.0	0.0	0.0	0.0	0.0	0.0

Estimate of any current year (FY 97) cost: \$ 0.0

**POSITIONS**

FULL-TIME						
PART-TIME						
TEMPORARY						

**ANALYSIS:** (Attach a separate page if necessary)  
 This bill will not have a fiscal impact on the component.

Prepared by: Marianne K. Burke, Director *Marianne K. Burke* Phone: 465-2515  
 Division: Insurance Date: 3/7/97  
 Approved by Commissioner: William L. Hensley *W. Hensley* Date: 3-7-97  
 Agency: Commerce and Economic Development

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# HOUSE COMMITTEE REPORT

(7)

Date Referred to Committee: March 6, 1997

FURTHER REFERRALS:

Judiciary

Date of Committee Action: 3/12/97

The LABOR AND COMMERCE Committee considered:

HB 179

HOUSE BILL NO. 179

FRATERNAL BENEFIT SOCIETIES

“An Act relating to fraternal benefit societies; and providing for an effective date.”

recommends it be replaced  
with the following committee substitute \_\_\_\_\_

the same title  
 a new title

additional referral to \_\_\_\_\_ Committee  
 attached amendment(s)

ADOPTS: \_\_\_\_\_ Letter of Intent

ATTACHES NEW FISCAL NOTE(S): (Dept) \_\_\_\_\_

APPROVES PREVIOUS: (Dept/Date) \_\_\_\_\_

fiscal note(s) DCE

fiscal note(s) \_\_\_\_\_

zero fiscal note(s) \_\_\_\_\_

zero fiscal note(s) \_\_\_\_\_

SIGNING WITH RECOMMENDATIONS	DP	DNP	NR	AM
<i>Gene Kahan</i>			X	
<i>John Anderson</i>	✓			
<i>John Sanders</i>	✓			
<i>Tom Brine</i>			X	
<i>Bill Hudson</i>			✓	
<i>Gae Kahan</i>	✓			
<i>U. Neal Kately</i>	✓			

CHAIR'S SIGNATURE

*U. Neal Kately*

3/12/97

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TO: Rep Rokeberg, Attn: Shirley Armstrong

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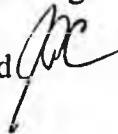
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### MEMORANDUM

March 12, 1997

**SUBJECT:** Sectional Summary of House Bill 179. (Work Order No. 20-LS0720\A)

**TO:** Representative Norman Rokeberg  
Attn: Shirley Armstrong

**FROM:** James P. Crawford   
Assistant Revisor

You have requested a sectional summary of the above-described bill.

As a preliminary matter, note that a sectional summary of a bill should not be considered an authoritative interpretation of the bill and the bill itself is the best statement of its contents.

Additionally, there appear to be no cases in Alaska that substantively discuss Fraternal Benefit Organizations in a way that could provide guidance on issues presented in the bill. Consequently, the division of insurance is likely to be one of the best resources to tap should questions about the bill arise.

Finally, rather than trying to discuss every point in each bill section exhaustively, I have limited discussion where possible to the main points of each section in the interests of readability and brevity.

**Section 1.** This section adds Article 1.

AS 21.84.005 - This section relates to representative forms of government of societies, which, among other things, must have a supreme governing body that is either an assembly or a board. In subsection (c), there is in my mind a question whether a supreme governing body board is in addition to or in place of a board of directors. However, once the sponsor decides this issue, minor language changes could clear up any ambiguity. *For purposes of comparison, some analogous or similar provisions in existing law are found in AS 21.84.900(4).*

AS 21.84.015 - This section requires that societies provide benefits as set out in AS 21.84.201 and operate for certain purposes. It also allows societies to adopt laws and rules

Representative Norman Rokeberg

March 12, 1997

Page 2

relating to its government. *For purposes of comparison, some analogous or similar provisions in existing law are found in AS 21.84.200 and AS 21.84.060(2).*

**Section 2.** This section adds 21.84.025, which relates to qualifications for membership, classes and types of membership, rights and privileges of and limitations on membership, and nonassignability of membership rights. *For purposes of comparison, some analogous or similar provisions in existing law are found in AS 21.84.180.*

**Section 3.** This section adds AS 21.84.035, which relates to location of the principal office; business transacted at meetings; minutes of the proceeding, which must conform to the English language requirement set out in AS 21.84.070; the official publication; synopses of annual statements; and grievance and complaint procedures. *For purposes of comparison, some analogous or similar provisions in existing law are found in AS 21.84.160 and 21.84.340(c).* Please note that subsection (c) is essentially restated in 21.84.465(e), found in bill section 26. Because this material fits better in the context of AS 21.84.465, the material should be removed from this section if the sponsor wants to eliminate what appears to be a redundancy.

By cross-referencing AS 21.84.070, the bill incorporates an English-language requirement for certain documents. I have recently (this morning at 8:00 am) become aware that a challenge to the constitutionality of an English-only law in Arizona reached the U.S. Supreme Court. Before reaching the Supreme Court, lower courts held the law, which required Arizona state employees to express the "official acts" of the state in English, to be unconstitutional. However, the Supreme Court vacated the lower court holdings as moot because the state employee resigned from state employment a day after notices of appeal were filed. US Sup Ct, No. 95-974, 3/3/97. I have not had time to research this issue more closely, but I think it is safe to say that the constitutionality of such laws is an open question in the Ninth Circuit, which encompasses Alaska. There may be a distinction between that case and the present situation in that the law in Arizona required use of English by public employees, where the law here requires the use of English by private organizations.

**Section 4.** This section adds AS 21.84.045, which provides that officers and members are not personally liable for a society's benefits; requires indemnification and reimbursement of certain persons, along with exceptions; allows purchase of insurance on behalf of directors, officers, employees, and agents for certain purposes; and provides limited immunity for certain persons serving without compensation. *For purposes of comparison, some analogous or similar provisions in existing law are found in AS 21.84.250.*

**Section 5.** This section adds AS 21.84.055, which allows a society to provide that laws may not be waived in certain circumstances, and AS 21.84.059, which relates to the process by which a society may amend its laws. *For purposes of comparison, some analogous or similar provisions in existing law are found in AS 21.84.150 and 21.84.140.*

**Section 6.** This section amends AS 21.84.060 by changing "society" to "domestic society"; by inserting a date relating to a domestic society's form of government; by deleting references to certain purposes of societies, which may now be found in AS 21.84.015(a)(2); and by changing "certificate" to "certificate of authority."

**Section 7.** This section amends AS 21.84.070, the most significant amendments being the increase in the amounts of bonds relating to the completion date of the organization of a society.

**Section 8.** This section amends AS 21.84.080 by changing "certificate" to "certificate of authority" and "society" to "domestic society."

**Section 9.** This section amends 21.84.090, the most significant amendments relating to requirements a society must satisfy before taking actions relating to incurring liabilities, issuing certificates, or paying certain benefits.

**Section 10.** This section amends AS 21.84.100 by changing "society" to "domestic society" and by changing "certificate" to "certificate of authority."

**Section 11.** This section amends AS 21.84.120 to change a date relating to an obligation for a society to reincorporate.

**Section 12.** This section amends AS 21.84.170(a) to provide that societies may operate not for profit institutions to further purposes permitted by AS 21.84.015.

**Section 13.** This section adds AS 21.84.175, which relates to reinsurance agreements by societies. *For purposes of comparison, some analogous or similar provisions in existing law are found in AS 21.84.310.*

**Section 14.** This section adds 21.84.185, which relates to procedures and requirements for consolidations and mergers between societies. *For purposes of comparison, some analogous or similar provisions in existing law are found in AS 21.84.500 and 21.84.510.*

**Section 15.** This section adds 21.84.195, which relates to plans of conversion from a fraternal benefit organization to a mutual life insurance company. *For purposes of comparison, some analogous or similar provisions in existing law are found in AS 21.84.520.*

**Section 16.** This section adds 21.84.201, which lists types of benefits a society may provide, requires a society to specify rules relating to persons who may be issued or covered by contractual benefits, and allows benefits on the lives of persons under the age of adult membership. *For purposes of comparison, some analogous or similar provisions in existing law are found in AS 21.84.200.*

Representative Norman Rokeberg

March 12, 1997

Page 4

**Section 17.** This section amends AS 21.84.230(a) to provide for irrevocable beneficiary designations.

**Section 18.** This section amends AS 21.84.230(c) to provide that benefit contract proceeds are payable to the owner of the benefit contract at the death of an insured person if the insured person was not the owner and if there are no beneficiaries.

**Section 19.** This section adds AS 21.84.255, which relates to benefit contracts. It describes materials comprising the benefit contract; it describes the effect on certificate owners and beneficiaries of amendments to a society's laws; it discusses certain persons below the age of majority; it describes requirements that apply if reserves of classes of certificates become impaired; it discusses requirements relating to certificates of benefit contracts; it discusses transferability of certain benefit contracts; and it discusses assignability of benefit contracts. *For purposes of comparison, some analogous or similar provisions in existing law are found in AS 21.84.260 and 21.84.270.*

**Section 20.** This section adds AS 21.84.265, which relates to the size of certain amounts and benefit values connected to certificates. These amounts and benefit values are treated differently based on the certificate's date of issuance. If the certificate was issued before a specified date, the size is set by the provision of laws applicable on the day before the effective date of the Act. Note that the Act has an effective date of January 1, 1998, assuming the effective date provision receives the required number of votes. On the other hand, if the certificate was issued on or after the specified date, the size is set by reference to interest rate and mortality tables authorized by state law and used in calculating similar benefits of life and health insurers. The pivotal specified date in this section is a date one year after the effective date of the act. *For purposes of comparison, some analogous or similar provisions in existing law are found in AS 21.84.220.*

**Section 21.** This section adds AS 21.84.275, which describes investments authorized for societies, including foreign and alien societies. *For purposes of comparison, some analogous or similar provisions in existing law are found in AS 21.84.330.*

**Section 22.** This section amends AS 21.84.320(a) by changing "contract" to "benefit contract."

**Section 23.** This section adds subsection (d) to AS 21.84.320. This subsection relates to the establishment and operation of separate accounts and contracts issued on a variable basis.

**Section 24.** This section adds AS 21.84.335, which provides that societies are governed by AS 21.84 but are exempt from all other provisions of the insurance laws of the state except for specific chapters and sections listed. These listed chapters and sections outside AS 21.84 apply to societies to the extent applicable unless they conflict with AS 21.84. *For purposes*

*of comparison, some analogous or similar provisions in existing law are found in AS 21.84.590.*

**Section 25.** This section adds 21.84.455, which relates to standards of valuation of certificates issued by societies. *For purposes of comparison, some analogous or similar provisions in existing law are found in AS 21.84.350.*

**Section 26.** This section adds AS 21.84.465, which requires the filing of an annual statement of certain information about the society; requires the communication of synopses of the statement to benefit members; and allows the director of the division of insurance to require more frequent filing of statements. Note that subsection (e) essentially restates AS 21.84.035(c), set out in bill section 3. *For purposes of comparison, some analogous or similar provisions in existing law are found in AS 21.84.340.*

**Section 27.** This section adds AS 21.84.475, which relates to licences and renewals. Certain societies are authorized to conduct business through June 30 immediately following the effective date of the Act, which has an effective date of January 1, 1998, assuming the effective date provision receives the required number of votes. This authorization relates (1) to societies authorized to conduct business on the effective date of the act, and (2) to societies that become licensed after the effective date but before July 1 immediately following the effective date. The authority of these societies may be renewed annually but terminates on the first day of the succeeding July, which is also the case for all other societies. However, issued licenses continue until a new license is issued or specifically refused. *For purposes of comparison, some analogous or similar provisions in existing law are found in AS 21.84.030.*

**Section 28.** This section adds AS 21.84.485, which allows the director of the division of insurance to examine societies in the manner authorized under AS 21.06.120 - 21.06.230 for examination of insurers. Note that AS 21.06 has additional sections relating to examination that this section does not reference. *For purposes of comparison, some analogous or similar provisions in existing law are found in AS 21.84.370, 21.84.380, and 21.84.390.*

**Section 29.** This section adds 21.84.495, which relates to the licensing of foreign or alien societies. *For purposes of comparison, some analogous or similar provisions in existing law are found in AS 21.84.040.*

**Section 30.** This section adds AS 21.84.535, which relates to suspension, revocation, or refusal of licenses of foreign or alien societies. *For purposes of comparison, some analogous or similar provisions in existing law are found in AS 21.84.050.*

**Section 31.** This section adds 21.84.565, which requires agents of societies to be licensed in accordance with AS 21.27, which relates to licensing requirements in the insurance

Representative Norman Rokeberg  
March 12, 1997  
Page 6

industry in Alaska. It also creates an exception to requirements of examination and licensing.

**Section 32.** This section adds 21.84.575, which subjects societies and agents to AS 21.36, relating to unfair methods of competition or unfair or deceptive acts or practices in the business of insurance. This section also clarifies that the application of AS 21.36 does not affect certain activities by societies.

**Section 33.** This section adds Article 7 to AS 21.84.

AS 21.84.625 - This section requires a society to appoint the director of the division of insurance as its representative for receiving service of process. *For purposes of comparison, some analogous or similar provisions in existing law are found in AS 21.84.490.*

AS 21.84.650 - This section provides specific penalties for certain acts and a general penalty for acts that constitute a violation of AS 21.84 that are not penalized elsewhere.

AS 21.84.675 - This section provides for judicial review of decisions and findings of the director of the division of insurance. *For purposes of comparison, some analogous or similar provisions in existing law are found in AS 21.84.550.*

AS 21.84.700 - This section creates exemptions from the application and effect of AS 21.84 for certain categories of associations offering certain kinds of benefits. However, this section also removes the exemptions in some circumstances and places restrictions on activities of certain exempt associations. Also, please note that subsection (f) provides that societies that are exempt from the provision of AS 21.84 are "exempt from all other provisions of the insurance laws of this state," also found in existing law. *For purposes of comparison, some analogous or similar provisions in existing law are found in AS 21.84.020.*

**Section 34.** This section amends four definitions in AS 21.84.900, the chapter's definitions section, and repeals one definition, which is "representative form of government." This phrase is now found in AS 21.84.005, set out bill section 1.

**Section 35.** This section adds nine defined terms or phrases to AS 21.84.900.

**Section 36.** This section repeals those sections from AS 21.84 that have not been retained.

**Section 37.** This section provides an effective date of January 1, 1998.

JPC:glc  
97-166.glc

Amendment #1

Following Line 7 on Page 18, insert the following:

Adopted

"(15) AS 21.54;  
(16) AS 21.56;"

Renumber existing (15) through (18) accordingly.

AMENDMENT

H.R. *Adopted*

OFFERED IN HOUSE LABOR AND COMMERCE COMMITTEE

BY ROKEBERG

TO: HB 179

PAGE 1, Line13 after "body":

INSERT: ", or any intermediate assembly"



March 12, 1997

Rep. Norman Rokeberg  
Chair, House Labor And Commerce  
State Capitol  
Juneau, AK 99801-1182

Dear Representative Rokeberg

I am writing to ask your support for a bill now pending in the Alaska House of Representatives that affects the future of the fraternal benefit system in this state. House Bill 179 would implement the provisions of the Model Fraternal Code of the National Fraternal Congress of America in Alaska.

Fraternal benefit societies are nonprofit, self-help membership organizations formed by people of common ethnic, religious, or vocation backgrounds or people holding similar moral, ethical, or patriotic beliefs. By law, fraternal benefit societies must operate on a lodge system, maintain a representative form of government and offer benefits solely to members and their dependants. The Model Fraternal Code is needed in Alaska to update the law governing fraternal benefit societies and modernize the authority for fraternal to offer meaningful benefits to members.

I ask for your support for House Bill 179 so that fraternal benefit societies can continue their work in addressing community needs in this state. Thank you for your consideration of this measure.

Best regards

*Louis N. Wood*  
Louis N. Wood, LUTC

## Official Comment

1. This section combines some of the duties previously included in Sections 5-114 and 5-109. Because a confirmer has the rights and duties of an issuer, this section applies equally to a confirmer and an issuer. See Section 5-107(a).

The standard of strict compliance governs the issuer's obligation to the beneficiary and to the applicant. By requiring that a "presentation" appear strictly to comply, the section requires not only that the documents themselves appear on their face strictly to comply, but also that the other terms of the letter of credit such as those dealing with the time and place of presentation are strictly complied with. Typically, a letter of credit will provide that presentation is timely if made to the issuer, confirmer, or any other nominated person prior to expiration of the letter of credit. Accordingly, a nominated person that has honored a demand or otherwise given value before expiration will have a right to reimbursement from the issuer even though presentation to the issuer is made after the expiration of the letter of credit. Conversely, where the beneficiary negotiates documents to one who is not a nominated person, the beneficiary or that person acting on behalf of the beneficiary must make presentation to a nominated person, confirmer, or issuer prior to the expiration date.

This section does not impose a bifurcated standard under which an issuer's right to reimbursement might be broader than a beneficiary's right to honor. However, the explicit deference to standard practice in Section 5-108(a) and (e) and elsewhere expands issuers' rights of reimbursement where that practice so provides. Also, issuers can and often do contract with their applicants for expanded rights of reimbursement. Where that is done, the beneficiary will have to meet a more stringent standard of compliance as to the issuer than the issuer will have to meet as to the applicant. Similarly, a nominated person may have reimbursement and other rights against the issuer based on this article, the UCP, bank-to-bank reimbursement rules, or other agreement or undertaking of the issuer. These rights may allow the nominated person to recover from the issuer even when the nominated person would have no right to obtain honor under the letter of credit.

The section adopts strict compliance, rather than the standard that commentators have called "substantial compliance," the standard arguably applied in *Banco Español de Crédito v. State Street Bank and Trust Company*, 385 F.2d 230 (1st Cir. 1967) and *Flagship Cruises Ltd. v. New England Merchants Nat. Bank*, 569 F.2d 699 (1st Cir. 1978). Strict compliance does not mean slavish conformity to the terms of the letter of credit. For example, standard practice (what issuers do) may recognize certain

presentations as complying that an unschooled layman would regard as discrepant. By adopting standard practice as a way of measuring strict compliance, this article indorses the conclusion of the court in *New Braunfels Nat. Bank v. Odiome*, 780 S.W.2d 313 (Tex.Ct.App. 1989) (beneficiary could collect when draft requested payment on 'Letter of Credit No. 86-122-5' and letter of credit specified 'Letter of Credit No. 86-122-S' holding strict compliance does not demand oppressive perfectionism). The section also indorses the result in *Tosco Corp. v. Federal Deposit Insurance Corp.*, 723 F.2d 1242 (6th Cir. 1983). The letter of credit in that case called for "drafts Drawn under Bank of Clarksville Letter of Credit Number 105." The draft presented stated "drawn under Bank of Clarksville, Clarksville, Tennessee letter of Credit No. 105." The court correctly found that despite the change of upper case "L" to a lower case "l" and the use of the word "No." instead of "Number," and despite the addition of the words "Clarksville, Tennessee," the presentation conformed. Similarly a document addressed by a foreign person to General Motors as "Jeneral Mctors" would strictly conform in the absence of other defects.

Identifying and determining compliance with standard practice are matters of interpretation for the court, not for the jury. As with similar rules in Sections 4A-202(c) and 2-302, it is hoped that there will be more consistency in the outcomes and speedier resolution of disputes if the responsibility for determining the nature and scope of standard practice is granted to the court, not to a jury. Granting the court authority to make these decisions will also encourage the salutary practice of courts' granting summary judgment in circumstances where there are no significant factual disputes. The statute encourages outcomes such as *American Coleman Co. v. Intrawest Bank*, 887 F.2d 1382 (10th Cir. 1989), where summary judgment was granted.

In some circumstances standards may be established between the issuer and the applicant by agreement or by custom that would free the issuer from liability that it might otherwise have. For example, an applicant might agree that the issuer would have no duty whatsoever to examine documents on certain presentations (e.g., those below a certain dollar amount). Where the transaction depended upon the issuer's payment in a very short time period (e.g., on the same day or within a few hours of presentation), the issuer and the applicant might agree to reduce the issuer's responsibility for failure to discover discrepancies. By the same token, an agreement between the applicant and the issuer might permit the issuer to examine documents exclusively by electronic or electro-optical means. Neither those agreements nor others like them explicitly made by issuers and applicants violate the terms of Section 5-108(a) or (b) or Section 5-103(c).

2. Section 5-108(a) balances the need of the issuer for time to examine the documents against the possibility that the examiner (at the urging of the applicant or for fear that it will not be reimbursed) will take excessive time to search for defects. What is a "reasonable time" is not extended to accommodate an issuer's procuring a waiver from the applicant. See Article 14c of the UCP.

Under both the UCC and the UCP the issuer has a reasonable time to honor or give notice. The outside limit of that time is measured in business days under the UCC and in banking days under the UCP, a difference that will rarely be significant. Neither business nor banking days are defined in Article 5, but a court may find useful analogies in Regulation CC, 12 CFR 229.2, in state law outside of the Uniform Commercial Code, and in Article 4.

Examiners must note that the seven-day period is not a safe harbor. The time within which the issuer must give notice is the lesser of a reasonable time or seven business days. Where there are few documents (as, for example, with the mine run standby letter of credit), the reasonable time would be less than seven days. If more than a reasonable time is consumed in examination, no timely notice is possible. What is a "reasonable time" is to be determined by examining the behavior of those in the business of examining documents, mostly banks. Absent prior agreement of the issuer, one could not expect a bank issuer to examine documents while the beneficiary waited in the lobby if the normal practice was to give the documents to a person who had the opportunity to examine those together with many others in an orderly process. That the applicant has not yet paid the issuer or that the applicant's account with the issuer is insufficient to cover the amount of the draft is not a basis for extension of the time period.

This section does not preclude the issuer from contacting the applicant during its examination; however, the decision to honor rests with the issuer, and it has no duty to seek a waiver from the applicant or to notify the applicant of receipt of the documents. If the issuer dishonors a conforming presentation, the beneficiary will be entitled to the remedies under Section 5-111, irrespective of the applicant's views.

Even though the person to whom presentation is made cannot conduct a reasonable examination of documents within the time after presentation and before the expiration date, presentation establishes the parties' rights. The beneficiary's right to honor or the issuer's right to dishonor arises upon presentation at the place provided in the letter of credit even though it might take the person to whom presentation has been

made several days to determine whether honor or dishonor is the proper course. The issuer's time for honor or giving notice of dishonor may be extended or shortened by a term in the letter of credit. The time for the issuer's performance may be otherwise modified or waived in accordance with Section 5-106.

The issuer's time to inspect runs from the time of its "receipt of documents." Documents are considered to be received only when they are received at the place specified for presentation by the issuer or other party to whom presentation is made.

Failure of the issuer to act within the time permitted by subsection (b) constitutes dishonor. Because of the preclusion in subsection (c) and the liability that the issuer may incur under Section 5-111 for wrongful dishonor, the effect of such a silent dishonor may ultimately be the same as though the issuer had honored, i.e., it may owe damages in the amount drawn but unpaid under the letter of credit.

3. The requirement that the issuer send notice of the discrepancies or be precluded from asserting discrepancies is new to Article 5. It is taken from the similar provision in the UCP and is intended to promote certainty and finality.

The section thus substitutes a strict preclusion principle for the doctrines of waiver and estoppel that might otherwise apply under Section 1-103. It rejects the reasoning in *Flagship Cruises Ltd. v. New England Merchants' Nat. Bank*, 569 F.2d 699 (1st Cir. 1978) and *Wing On Bank Ltd. v. American Nat. Bank & Trust Co.*, 457 F.2d 328 (5th Cir. 1972) where the issuer was held to be estopped only if the beneficiary relied on the issuer's failure to give notice.

Assume, for example, that the beneficiary presented documents to the issuer shortly before the letter of credit expired, in circumstances in which the beneficiary could not have cured any discrepancy before expiration. Under the reasoning of *Flagship* and *Wing On*, the beneficiary's inability to cure, even if it had received notice, would absolve the issuer of its failure to give notice. The virtue of the preclusion obligation adopted in this section is that it forecloses litigation about reliance and detriment.

Even though issuers typically give notice of the discrepancy of tardy presentation when presentation is made after the expiration of a credit, they are not required to give that notice and the section permits them to raise late presentation as a defect despite their failure to give that notice.

4. To act within a reasonable time, the issuer must normally give notice without delay after the examining party makes its decision. If the examiner decides to dishonor on the first day, it would be obliged to notify the beneficiary shortly thereafter, perhaps on the same business day. This rule accepts the reasoning in cases such as *Datapoint Corp. v. M & I Bank*, 665 F. Supp. 722 (W.D. Wis. 1987) and *Esso Petroleum Canada, Div. of Imperial Oil, Ltd. v. Security Pacific Bank*, 710 F. Supp. 275 (D. Ore. 1989).

The section deprives the examining party of the right simply to sit on a presentation that is made within seven days of expiration. The section requires the examiner to examine the documents and make a decision and, having made a decision to dishonor, to communicate promptly with the presenter. Nevertheless, a beneficiary who presents documents shortly before the expiration of a letter of credit runs the risk that it will never have the opportunity to cure any discrepancies.

5. Confirmers, other nominated persons, and collecting banks acting for beneficiaries can be presenters and, when so, are entitled to the notice provided in subsection (b). Even nominated persons who have honored or given value against an earlier presentation of the beneficiary and are themselves seeking reimbursement or honor need notice of discrepancies in the hope that they may be able to procure complying documents. The issuer has the obligations imposed by this section whether the issuer's performance is characterized as "reimbursement" of a nominated person or as "honor."

6. In many cases a letter of credit authorizes presentation by the beneficiary to someone other than the issuer. Sometimes that person is identified as a "payor" or "paying bank," or as an "acceptor" or "accepting bank," in other cases as a "negotiating bank," and in other cases there will be no specific designation. The section does not impose any duties on a person other than the issuer or confirmer, however a nominated person or other person may have liability under this article or at common law if it fails to perform an express or implied agreement with the beneficiary.

7. The issuer's obligation to honor runs not only to the beneficiary but also to the applicant. It is possible that an applicant who has made a favorable contract with the beneficiary will be injured by the issuer's wrongful dishonor. Except to the extent that the contract between the issuer and the applicant limits that liability, the issuer will have liability to the applicant for wrongful dishonor under Section 5-111 as a matter of contract law. A good faith extension of the time in Section 5-108(b) by agreement between the issuer and beneficiary binds the applicant even if the applicant is not consulted or does not consent to the extension.

The issuer's obligation to dishonor when there is no apparent compliance with the letter of credit runs only to the applicant. No other party to the transaction can complain if the applicant waives compliance with terms or conditions of the letter of credit or agrees to a less stringent standard for compliance than that supplied by this article. Except as otherwise agreed with the applicant, an issuer may dishonor a noncomplying presentation despite an applicant's waiver.

Waiver of discrepancies by an issuer or an applicant in one or more presentations does not waive similar discrepancies in a future presentation. Neither the issuer nor the beneficiary can reasonably rely upon honor over past waivers as a basis for concluding that a future defective presentation will justify honor. The reasoning of *Courtaulds of North America Inc. v. North Carolina Nat. Bank*, 528 F.2d 802 (4th Cir. 1975) is accepted and that expressed in *Schweibish v. Pontchartrain State Bank*, 389 So.2d 731 (La.App. 1980) and *Titanium Metals Corp. v. Space Metals, Inc.*, 529 P.2d 431 (Utah 1974) is rejected.

8. The standard practice referred to in subsection (e) includes (i) international practice set forth in or referenced by the Uniform Customs and Practice, (ii) other practice rules published by associations of financial institutions, and (iii) local and regional practice. It is possible that standard practice will vary from one place to another. Where there are conflicting practices, the parties should indicate which practice governs their rights. A practice may be overridden by agreement or course of dealing. See Section 1-205(4).

9. The responsibility of the issuer under a letter of credit is to examine documents and to make a prompt decision to honor or dishonor based upon that examination. Nondocumentary conditions have no place in this regime and are better accommodated under contract or suretyship law and practice. In requiring that nondocumentary conditions in letters of credit be ignored as surplusage, Article 5 remains aligned with the UCP (see UCP 500 Article 13c), approves cases like *Pringle-Associated Mortgage Corp. v. Southern National Bank*, 571 F.2d 871, 874 (5th Cir. 1978), and rejects the reasoning in cases such as *Sherwood & Roberts, Inc. v. First Security Bank*, 682 P.2d 149 (Mont. 1984).

Subsection (g) recognizes that letters of credit sometimes contain nondocumentary terms or conditions. Conditions such as a term prohibiting "shipment on vessels more than 15 years old," are to be disregarded and treated as surplusage. Similarly, a requirement that there be an award by a "duly appointed arbitrator" would not require the issuer to determine whether the arbitrator had been "duly appointed." Likewise a term in a

standby letter of credit that provided for differing forms of certification depending upon the particular type of default does not oblige the issuer independently to determine which kind of default has occurred. These conditions must be disregarded by the issuer. Where the nondocumentary conditions are central and fundamental to the issuer's obligation (as for example a condition that would require the issuer to determine in fact whether the beneficiary had performed the underlying contract or whether the applicant had defaulted) their inclusion may remove the undertaking from the scope of Article 5 entirely. See Section 5-102(a)(10) and Comment 6 to Section 5-102.

Subsection (g) would not permit the beneficiary or the issuer to disregard terms in the letter of credit such as place, time, and mode of presentation. The rule in subsection (g) is intended to prevent an issuer from deciding or even investigating extrinsic facts, but not from consulting the clock, the calendar, the relevant law and practice, or its own general knowledge of documentation or transactions of the type underlying a particular letter of credit.

Even though nondocumentary conditions must be disregarded in determining compliance of a presentation (and thus in determining the issuer's duty to the beneficiary), an issuer that has promised its applicant that it will honor only on the occurrence of those nondocumentary conditions may have liability to its applicant for disregarding the conditions.

10. Subsection (f) condones an issuer's ignorance of "any usage of a particular trade"; that trade is the trade of the applicant, beneficiary, or others who may be involved in the underlying transaction. The issuer is expected to know usage that is commonly encountered in the course of document examination. For example, an issuer should know the common usage with respect to documents in the maritime shipping trade but would not be expected to understand synonyms used in a particular trade for product descriptions appearing in a letter of credit or an invoice.

11. Where the issuer's performance is the delivery of an item of value other than money, the applicant's reimbursement obligation would be to make the "item of value" available to the issuer.

12. An issuer is entitled to reimbursement from the applicant after honor of a forged or fraudulent drawing if honor was permitted under Section 5-109(a).

13. The last clause of Section 5-108(i)(5) deals with a special case in which the fraud is not committed by the beneficiary, but is committed by a

stranger to the transaction who forges the beneficiary's signature. If the issuer pays against documents on which a required signature of the beneficiary is forged, it remains liable to the true beneficiary.

#### SECTION 5-109. FRAUD AND FORGERY.

(a) If a presentation is made that appears on its face strictly to comply with the terms and conditions of the letter of credit, but a required document is forged or materially fraudulent, or honor of the presentation would facilitate a material fraud by the beneficiary on the issuer or applicant:

(1) the issuer shall honor the presentation, if honor is demanded by (i) a nominated person who has given value in good faith and without notice of forgery or material fraud, (ii) a confirmer who has honored its confirmation in good faith, (iii) a holder in due course of a draft drawn under the letter of credit which was taken after acceptance by the issuer or nominated person, or (iv) an assignee of the issuer's or nominated person's deferred obligation that was taken for value and without notice of forgery or material fraud after the obligation was incurred by the issuer or nominated person; and

(2) the issuer, acting in good faith, may honor or dishonor the presentation in any other case.

(b) If an applicant claims that a required document is forged or materially fraudulent or that honor of the presentation would facilitate a material fraud by the beneficiary on the issuer or applicant, a court of

Charlie Miller  
230 S. Franklin, #611  
Juneau, AK 99801  
(907) 463-5062

MAR 13 1997

5:35pm

MEMO

DATE: 3/13/97  
TO: Shirley Armstrong  
FROM: Charlie  
RE: CSHB179 Amendment

---

I think that this is what Norm wanted from the NFCA on the amendment. Let me know if you need anything else. Thanks again for all your help.

3/13/97

Charlie Miller  
230 S Franklin, #611  
Juneau, AK 99801  
463-5062

Representative Norman Rokeberg  
State Capitol, Room 24  
Juneau, AK 99801-1182

Dear Chairman Rokeberg:

You requested a written explanation of amendment number 2, offered on HB179, during the House Labor & Commerce Committee Hearing on March 12.

Amendment: Page 1, Line 13 after "body" insert ".or any intermediate assembly"

The supreme governing body of a fraternal benefit society must be selected by the members of the society. In the case of some societies, there are intermediate assemblies elected in the process of electing the supreme governing body. This amendment clarifies that such intermediate assemblies must also be composed of members of the society.

Please let me know if this is what you needed. Thank you for the efforts of your staff and yourself on this proposed legislation.

Sincerely,



Charlie Miller

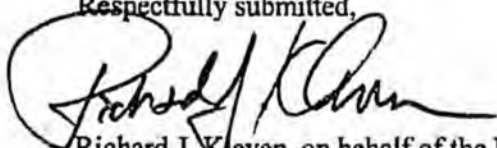
Model Fraternal Code  
State of Alaska  
March 10, 1997  
Page 3

This Model Fraternal Code has been enacted in 33 states and four other states have enacted its essential features. There are no domestic fraternal benefit societies licensed in Alaska, but several societies from other states are. Those societies have over 8,000 members in Alaska, and through their 45 local lodges in your state in 1995 held 818 fraternal events, performed 9,587 fraternal acts of service represented by 57,988 hours of service. In addition, Alaska licensed fraternal benefit societies disbursed \$227,488 for fraternal, charitable and benevolent activities for the citizens of Alaska in 1995.

The revisions contained in the Model Fraternal Code will be of benefit to the Alaska Division of Insurance, to the licensed fraternal benefit societies in Alaska, to their 8,000+ members in the state, to the Alaska citizens who may in the future become members of a fraternal benefit society, and to the communities which we also serve.

Therefore, on behalf of the NFCA, I respectfully request that House Bill 179 and Senate Bill 119 be favorably considered and enacted by the Legislature of Alaska.

Respectfully submitted,



Richard J. Kleven, on behalf of the National Fraternal Congress of America  
March 1997

John L. George & Associates  
3328 Fritz Cove Road  
Juneau, Alaska 99801  
Tel. 907 789-0172 Fax 907 789-6964

March 10, 1997

The Honorable Norman Rokeberg  
Chairman House Labor and Commerce Committee  
House of Representatives  
State Capitol  
Juneau, Alaska 99801

Reference: HB 179

Dear Representative Rokeberg,

On behalf of the American Council of Life Insurance, I would like to express our support for HB 179 which up dates the insurance statutes relating to fraternal benefit societies. Fraternal provide insurance products to their members in competition with products provided by stock and mutual life insurance companies. Although fraternal serve a relatively small and specialized membership, we believe that they are an important provider of coverage to their members.

The proposed legislation modernizes the current statutes and does not create a significant competitive advantage or disadvantage for fraternal benefit societies. Although I do not plan to testify on this bill before your committee, I wanted to express to you that we support passage of this legislation.

Sincerely,



John L. George

# LEGAL SERVICES

DIVISION OF LEGAL AND RESEARCH SERVICES  
LEGISLATIVE AFFAIRS AGENCY  
STATE OF ALASKA

MAR 05 1997

(907) 465-3867 or 465-2450  
FAX (907) 465-2029  
Mail Stop 3101

130 Seward Street, Suite 409  
Juneau, Alaska 99801-2105

## MEMORANDUM

March 4, 1997

**SUBJECT:** Bill on letters of credit (Work Order No. 20-LS0644\A)

**TO:** Representative Norman Rokeberg, Chair  
House Labor and Commerce Committee

**FROM:** *TB*  
Theresa Bannister  
Legislative Counsel

This memo accompanies a draft of the bill described above. The draft consists of HB 553 from the 19th legislature and, per your request in the work order, the changes determined to be necessary after reviewing the letters of Mr. Peterson and Mr. Kurtz and consulting with them and with Mr. McCabe (NCCUSL) on the more difficult ones.

The following describes the changes made (excluding technical changes necessitated by, e.g., recent amendments). The descriptions are identified according to the numbers where they appear in my original cover letter of April 10, 1996.

2. AS 45.05.102(a). In (a)(5) moved "timely" to its position in the NCCUSL draft. In (a)(6)(2) changed to "the standard practice." Also changed to "the standard practice" wherever the term occurs in the bill.
6. AS 45.05.107(c). Changed "the adviser" to "the person requested to advise," after talking with Mr. McCabe (NCCUSL).
8. AS 45.05.108(a). Restored the NCCUSL language "so to comply." Although the use of "so" is disfavored under the legislative drafting style, the additional language suggested to make the bill draft's language accurate appeared to require more interpretation than seems appropriate for a NCCUSL 'ill.
10. - 11. AS 45.05.108(h) - (i). Restored "who" to "that" here and throughout the bill.
12. AS 45.05.109(a). Restored the "and." Deleted the comma after "demanded" in (a)(1). Restored the past perfect and past tenses.
13. AS 45.05.109(a)(1)(B). Restored "its confirmation."
17. AS 45.05.109(b). Restored the NCCUSL version using "only."

Representative Norman Rokeberg

March 4, 1997

Page 2

19. AS 45.05.110(a). Restored "if its presentation."
22. AS 45.05.111(e). Rewrote AS 45.05.111(e) to operate under Court Rules 79 and 82. Deleted court rule references in the title and bill section describing the court rule changes. A change in (d) is not needed.
24. AS 45.05.113(b). Restored "upon compliance with." Restored "the standard practice referred to in."
26. AS 45.05.114(a). After talking to Mr. McCabe (NCCUSL), restored NCCUSL's second sentence, but substituted "the beneficiary's" for "its."
29. AS 45.05.114(e). After talking to Mr. McCabe (NCCUSL), in the last sentence placed "and its perfection," after "security interest" and deleted "and perfection" after "creation." "Perfection" should not modify "other assignment."
30. AS 45.05.116(b). Corrected spelling of "judicial."
31. AS 45.05.116(c). No change made.
33. AS 45.05.117(d). Added "of subrogation stated in."
36. Effective date section. Made the effective date the later date of January 1, 1998. If a bill is passed in the last days of the legislative session, the bill may not get to the governor's desk for a while, and there is a possibility that the bill would be signed into law after July 1, 1997.

If I may be of further assistance, please advise.

TLB:jd.:glc

97-133.jdr

Enclosure

# STATE OF ALASKA

## DEPARTMENT OF COMMERCE AND ECONOMIC DEVELOPMENT

DIVISION OF INSURANCE

MAR 13 1997  
*Received 4:55 PM*  
TONY KNOWLES, GOVERNOR *sh*

P.O. BOX 110805  
JUNEAU, ALASKA 99811-0805  
PHONE: (907) 465-2515  
FAX: (907) 465-3422  
TDD: (907) 465-5437

March 13, 1997

Representative Norman Rokeberg  
Alaska House of Representatives  
House Labor & Commerce Committee  
State Capitol  
Juneau, AK 99801-1182

Dear Representative Rokeberg:

**RE: Amendment to HB 179**

Following my testimony at House Labor & Commerce yesterday on HB 179, you asked that I provide a written explanation of the amendment I offered during my testimony.

The chapter of law dealing with fraternal benefit societies (fraternals), AS 21.84, contains a section that references other sections and chapters in the insurance code applicable to a fraternal. The section in existing law is AS 21.84.590. The section in HB 179 replacing Sec 590 is AS 21.84.335 which appears on pages 17 and 18 of the bill. This section is necessary because the structure and purpose of a fraternal is substantially different from other life and annuity insurers.

A recently effective federal law, the Health Insurance Portability and Accountability Act of 1996 (PL 104-191) also referred to as the Kassebaum/Kennedy Bill, specifically addresses group health insurance products issued by a fraternal. These products are impacted by the new federal law. The treatment of issues addressed by the federal law, to the extent they are or will be addressed in Alaska law, appears in two chapters that are not currently listed in the existing AS 21.84.590 or the proposed AS 21.84.335. To avoid any potential conflict for fraternals with the federal law, we need only add the following language on Page 18, Line 7 of the bill and renumber (15)-(18):

“(15) AS 21.54;  
(16) AS 21.56;”

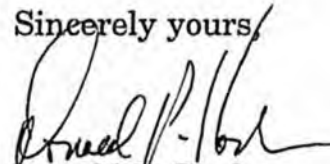
Representative Rokeberg

-2-

March 13, 1997

If you have any questions, you may reach me at (907) 465-2577 or at don\_koch@commerce.state.ak.us on the Internet.

Sincerely yours,

A handwritten signature in black ink, appearing to read "Donald P. Koch", written in a cursive style.

Donald P. Koch  
Chief of Market Surveillance



ANCHORAGE  
ECONOMIC  
DEVELOPMENT  
CORPORATION

Wes Coyner - Banks

OK

No. 553 (19<sup>th</sup>) →

Letter of Credit  
transaction

authenticity I w transaction (review)

Drafted (Terry Bowler)

Jerry Kurtz (Burr/Peace/Kurtz)

550 West 7th Avenue, Suite 1130 • Anchorage, AK 99501 • Telephone (907) 258-3700 • FAX (907) 258-6646

276-6100

uwitem (aw)



ANCHORAGE  
ECONOMIC  
DEVELOPMENT  
CORPORATION

Tony Brownstein

adopted

Peterson 2/20/96

9/26/96

10/4/96

no sleeper

no controversy

BZ Law Section of ABA

John Tindall (inactive)  
(ANC)

John Beanel (Bank)

550 West 7th Avenue • Suite 1130 • Anchorage, AK 99501 • Telephone (907) 258-3700 • FAX (907) 258-6646

**Comparison of Sections in the Alaska Bill Amending  
 AS 21:84 with Corresponding Sections in the  
 NFCA Model Fraternal Code**

<u>Alaska Draft</u>	<u>MFC Section</u>	<u>MFC Counterpart</u>
new 21.84.005	3	Representative form of government
21.84.025	6	Membership
21.84.035	7	Location of office
21.84.045	8	No personal liability - indemnity
21.84.055	9	Waiver
21.84.059	11	Amendments to laws
21.84.060	10	Articles of Incorporation
21.84.070	10	Filing Arts; bond increased - OK
21.84.080	10	Completing organization - 1 year
21.84.090	10	Solicitations - \$150,000 premium - OK
21.84.110	10	Certificate of compliance
21.84.120	10	Corporate powers retained
21.84.170(a)	11	Institutions
21.84.175	13	Reinsurance
21.84.185	14	Consolidations and mergers
21.84.195	15	Conversion to mutual insurer
21.84.201	16	Benefits
21.84.230(a)	17	Beneficiaries - owner; irrevocable beneficiary
21.84.230(c)	17	Payable to owner - OK
21.84.255	19	Benefit contract; MFC 19(f) included - OK
21.84.265	20	Nonforfeitures - MFC - OK
21.84.275	21	Investments - OK
21.84.320(a)	22(a)	Funds - MFC
21.84.320(d)	22(c)	Separate accounts - MFC
21.84.335	23	Exemptions - other applicable provisions (same as present law 21.84.010 and 21.84.590)
21.84.455	25	Valuation - MFC - OK
21.84.465	26	Reports - annual statement
21.84.475	27	License
21.84.485	28	Examinations - MFC - OK
21.84.495	29	Foreign/alien society
21.84.535	31	Suspension of foreign/alien society
21.84.565	33	Agents - (c) contains older MFC part-time exemptions
21.84.575	34	Trade practices
21.84.625	35	Service of process - MFC
21.84.650	37	Penalties
21.84.700	38	Exempt societies
21.84.900	4	Definitions
(1)	1	"fraternal benefit society"
(2)	2	"lodge system"
(3)	4	"premiums"
(4)	3	"representative form of government"
(5)	1	"society"
6 et seq.	4	include MFC 4 definitions

These sections of existing Alaska law remain in force intact:

- 21.84.130(a) - "After July 1, 1967, an unincorporated or voluntary association may not be permitted to transact business in this state as a fraternal benefit society."
- 21.84.230(b) - (MFC 17(b)) - Funeral benefit limited to \$500
- 21.84.240 - (MFC 18) - Immunity of benefits from attachment
- 21.84.400 - (MFC 24) - Tax exemption
- 21.84.530 - (MFC 30) - Injunction or liquidation [domestic society]
- 21.84.540 - (MFC 32) - Petition for injunction

A PROPOSAL FOR ENACTMENT OF THE MODEL FRATERNAL CODE  
OF THE NATIONAL FRATERNAL CONGRESS OF AMERICA  
IN LIEU OF CHAPTER 84 OF THE ALASKA INSURANCE CODE

A. The legislative history of the antecedents to Chapter 84 of the Alaska Insurance Code.

Alaska enacted a new comprehensive Insurance Code in 1966 as Title 21 of the Statute Law of Alaska (Chapter 120, SLA 1966). Chapter 84 of Title 21, Sections 21.84.010 to 21.84.590 and 21.84.900, govern fraternal benefit societies. The provisions in Chapter 84 as enacted in 1966 were nearly identical to the text of the Uniform Fraternal Code of 1962 that had been drafted and approved by the National Fraternal Congress of America (NFCA) and the National Association of Insurance Commissioners. Twenty-four other states and Puerto Rico also adopted the Uniform Fraternal Code.

Present Chapter 84 has been amended several times since 1966:

<u>Section</u>	<u>Caption</u>	<u>Amendment Date</u>
21.84.010	Scope	Sec. 211, C. 67, 1992
21.84.030	License	Sec. 21, C. 26, 1985
21.84.210	Children	Sec. 22, C. 21, 1985
21.84.220	Nonforfeiture	Secs. 4,5, C. 28, 1984
21.84.290	(repealed)	Sec. 223, C. 67, 1992
21.84.340	Statement	Sec. 22, C. 26, 1985
21.84.350	Valuation	Sec. 6, C. 28, 1984 Sec. 212, C. 67, 1992
21.84.410 to		
21.84.460	(repealed)	Sec. 223, C. 67, 1992
21.84.470	Misrepresentation	Sec. 19, C. 149, 1984
21.84.480	Discrimination	Sec. 213, C. 67, 1992
21.84.490	Process	Sec. 24, C. 26, 1985
21.84.560 to		
21.84.580	(repealed)	Sec. 223, C. 67, 1992
21.84.590	Applicability of Code	Sec. 2, C. 40, 1981 Sec. 2, C. 45, 1981 Sec. 20, C. 149, 1984 Sec. 25, C. 26, 1985

21.84.900

Definitions(added)

Sec. 36, C. 50, 1989

Sec. 3, C. 106, 1990

Sec. 214, C. 67, 1992

Sec. 215, C. 67, 1992

Senate Bill S. 319. Laws of 1996 also amended various sections non-substantively in Chapter 84 [S. 319, Secs. 98 to 102].

In 1980, the NFCA undertook a project to revise and update the 1962 Uniform Code. The 1983 Model Fraternal Code draft was the result, adopted by the NFCA at its Annual Convention in Denver, Colorado, in October 1983.

Since then, the 1983 Model Fraternal Code (MFC), with some drafting changes to accommodate requests of the particular Insurance Department, has been enacted in thirty-one states:

Arizona	Illinois	Minnesota	North Dakota	Virginia
Arkansas	Indiana	Missouri	Oklahoma	Washington
Colorado	Iowa	Montana	Oregon	Wyoming
Florida	Kansas	Nebraska	Pennsylvania	
Georgia	Kentucky	Nevada	Rhode Island	
Hawaii	Louisiana	New Mexico	South Dakota	
Idaho	Michigan	North Carolina	Tennessee	

Fifteen of those states, like Alaska, had previously enacted the Uniform Code. California, Utah and Wisconsin also have modern fraternal benefit societies laws containing the essential features of the NFCA 1983 Model Code. MFC legislation is currently being considered in the District of Columbia, Maryland and New York. An MFC bill in Ohio, HB-468, has already passed the House and is pending in the Senate.

B. Why does Alaska need a new fraternal benefit society law?

Today's environment of rapid changes in the insurance industry demand that there also be major changes in the laws regulating insurers.

While one particular fraternal benefit society may be affected by current changes to a greater or lesser degree than would another society, no society is entirely immune from the environment in which it operates. When changes in the environment occur, each society must carefully evaluate the nature of the changes. Implicit

in this consideration is that each society has options from which to choose alternate courses of action. It is one thing to choose not to exercise an option and quite another to have no options from which to choose.

The 1983 Model Fraternal Code of the NFCA meets the challenges of the present and future in the following ways. The most sweeping additions to the revised code would give fraternal clear authority to own subsidiary corporations and to establish the separate accounts necessary for offering variable life insurance and variable annuities. Another addition would assure that the benefit authority of fraternal would be able to keep pace with any new authorities granted to commercial life insurers in the future.

In addition to these major changes, the revised code:

- Improves the presentation of fraternal purposes and characteristics through rewriting and reorganization.
- Maintains key fraternal characteristics--lodge system, representative form of government, membership--and traditional elements such as ritual.
- Improves provisions regarding juvenile contracts, designation of irrevocable beneficiaries, assignment of contracts and use of contracts for third-party insurance situations--to make contracts more useful to members in their personal, financial and tax planning.
- Integrates some regulatory provisions with commercial insurance standards to assure up-to-date regulation, while maintaining specific exceptions for unique fraternal practices.
- Uses updated language, uniform definitions, gender-neutral references, and consistent terminology.

C. The following is a section by section comparison of the MFC bill draft of new section numbers in Chapter 84 with corresponding sections in present Chapter 84:

MFC Section	Ch. 84 Section	<u>Caption and Commentary</u>
21.84.1010	21.84.900(1)	Fraternal Benefit Society description is substantially the same as present law.
21.84.1020	21.84.900(2)	Lodge System description is substantially the same as present law. Subsection (b) is essentially the same as present Section 21.84.210(a) relating to branches for children.

21.84.1030	21.84.900(4)	<p>Representative Form of Government - is similar to present law. Subsection (a) clearly recognizes two types of supreme governing bodies: (1) an assembly consisting of delegates elected by the members, and (2) a board elected directly by the members. Voting by mail has been authorized. At least one foreign society licensed in Alaska has the latter form of government.</p>
21.84.1040	21.84.900	<p>Terms Used -- Defines terms commonly used in the chapter. This section includes the definition of "premiums" and "society" in present Section 21.84.900 (3) and (5). The other definitions in that section are found in MFC Sections 21.84.1010, 21.84.1020 and 21.84.1030.</p>
21.84.1050	21.84.060(2)	<p>Purposes and Powers -- contains a listing of named purposes for which a society may be organized and states that these purposes may be carried out directly by the society, or indirectly through subsidiaries or affiliated organizations. The named purposes in subsection (a)(2) are the same as recited in present Section 21.84.060(2) with "patriotic" added. Owning subsidiary corporations which engage in activities beyond the stated purposes would be permitted only in accordance with the investment laws of the state of domicile of a society and whatever subsidiary authority can be derived therefrom. MFC Section 21.84.1210 covers investments generally, specifically authorizing societies to invest their funds in investments authorized for life insurers. The organization requirements are contained in MFC Section 21.84.1100.</p>
21.84.1060	21.84.180	<p>Membership -- emphasizes the importance of fraternalism as membership organizations, and gives societies authority to set eligibility standards and the rights and privileges of each membership class. This section stresses the society's right and duty to set membership qualifications. A conscious effort has been made to divorce concepts of membership from concepts of insurance, the latter taken up in MFC Section 21.84.1160 - Benefits, and Section 21.84.1190 - The Benefit Contract.</p>

21.84.1070	21.84.160; .340(c)	Location of Office, Meetings, Communications--Subsection (a) is similar to present law, except that a society may hold a meeting where it has only one branch (instead of five). Subsection (b)(1) permits notices, etc. to be distributed to members through the society's official publication. Subsection (b)(2) is similar to present section 21.84.340(c) (requiring the mailing of a synopsis of the annual statement to a society's members). Subsection (c) contains statutory authorization for grievance procedures.
21.84.1080	21.84.250	No Personal Liability-Subsection (a) is similar to present law. Subsections (b) and (c) provide authorization for indemnification of directors, officers, etc. and for the purchase of directors and officers liability insurance. Subsection (d) provides immunity from liability for directors, officers and employees serving without compensatio..
21.84.1090	21.84.150	Waiver - provides that no subordinate body, officers or members may waive any provisions of the laws of the society, similar to present law.
21.84.1100	21.84.-060 to 21.84.100	<p>Organization - This section includes all organizational requirements of present law, and increases the bond requirement to not less than \$300,000 nor more than \$1,500,000 as required by the Director. The amount of initial premiums required has been raised to \$150,000. The purpose of these changes is to bring the organizational requirements more in line with contemporary economic realities. However, to our knowledge no domestic society has ever been organized in Alaska.</p>
21.84.1110	21.84.140	Amendments to Laws - provides for submission and approval of amendments to the laws of a domestic society, and the filing of any such amendments by licensed foreign or alien societies, the same as present law.
21.84.1120	21.84.170	Institutions -- permits societies to operate and maintain organizations relevant to their society's purposes, similar to present law. Subsection (b) is the same as present Section 21.84.170(c)

providing that a society may not own or operate funeral homes or undertaking establishments.

21.84.1130	21.84.130	Reinsurance - is substantially the same as present law, but provides that a society may not reinsure the business of another society other than in a consolidation or merger.
21.84.1140	21.84.500; .510	Consolidations and mergers - is substantively the same as present law.
21.84.1150	21.84.520	Conversion of Fraternal Benefit Society into Mutual Life Insurance Company - is similar to present law.
21.84.1160	21.84.200; .210	Benefits -- lists authorized benefits the same as present law, but without the \$300 limit on tombstone benefits, and includes benefits for children and adults instead of providing for them in separate sections. The words "health care" are used in subsection (a)(4) to reflect the amendment enacted by section 102 of S. 316, Laws of 1996. Subsection (a)(7) provides that a society may issue benefits as authorized for life insurers, and which are not inconsistent with the fundamental characteristics of fraternal benefit societies. The question of contractual benefits is addressed in subsection (b).
21.84.1170	21.84.230	Beneficiaries -- places control of beneficiary designations in the hands of each society. This section covers the various matters contained in present law, subsection (c) also providing that if the owner of the certificate is other than the insured, the proceeds shall be paid to the owner.
21.84.1180	21.84.240	Benefits Not Attachable - is the same as present law.
21.84.1190	21.84.260 to 21.84.300 and 21.84.190	

The Benefit Contract -- subsections (a) and (b) preserve the "open contract" concept of fraternal certificates contained in present Section 21.84.260(a) and (c). Likewise, the traditional "maintenance of solvency" provision in present Section 21.84.190 is preserved in subsection (d). Subsection (f) requires all fraternal certificates to be filed with the Director, the same as present law, and all certificates

issued after one year from the effective date of the Model Code must conform to the requirements for like policies issued by commercial life and health insurers. The provision in present Section 21.84.300(c) that a filing of a health certificate shall be considered approved unless disapproved within 60 days has been inserted in subsection (f) and made applicable also to a filing of a life certificate.

Subsection (f) makes unnecessary the inclusion of the text of present Sections 21.84.270 to .300 (standard and prohibited provisions) because fraternal certificates will be subject to the same general requirements for commercial life and health insurance company policies.

Subsections (g) and (h) pertain to control over juvenile contracts, and the conditions under which benefit contracts may be assigned.

21.84.1200      21.84.220; 21.84.350 & 21.84.1250

Nonforfeiture Benefits (Section 21.84.1200), and Valuation (Section 21.84.1250) - The thrust of these two sections is essentially the same as present law relating to calculation of nonforfeiture benefits and valuation of reserves. They provide that existing law shall apply to outstanding certificates, but that for certificates issued on or after one year from the effective date of the Model Code, societies must use at least the Commissioner's 1941 CSO Table. These two sections incorporate the authorization in present Section 21.84.220(d) and 21.84.350(j) that a society may calculate nonforfeiture benefits and value reserves of newly issued policies on any more recent mortality table authorized for use by commercial life insurance companies.

21.84.1210      21.84.330

Investments- This section is the same as present law.

21.84.1220      21.84.320

Funds - Subsections (a) and (b) are the same as in present law. Subsection (c) gives societies specific authority to create separate accounts. This authority is new. It will give fraternal the ability to offer members variable benefits. If variable benefits are subject to federal securities laws, the supreme governing body is authorized to exclude these forms of benefits from the "open contract" and

"maintenance of solvency" requirements in subsections (b) and (d) of MFC Section 21.84.1190. The supreme governing body is also empowered to authorize that separate, independent control be set up over such accounts should that be necessary or desirable. The text of present Section 21.84.320(c) would be obsolete and unnecessary because of the reserve valuation requirements in MFC Section 21.84.1250.

21.84.1230      21.84.010 and 21.84.590 - Applicability of other code provisions.

Subsection (a) is the same as present Section 21.84.010. Subsection (b) is the same as 21.84.590 with explanatory captions added for clarity.

21.84.1240      21.84.400      Taxation - is the same as present law.

21.84.1250      21.84.350      Valuation - See comment under MFC Section 21.84.1200. The text of present Section 21.84.350 would be obsolete and unnecessary because of the modern valuation requirements in MFC Section 21.84.1250.

21.84.1260      21.84.340; .350; .360

Reports - Subsection (a) is the same as present Section 21.84.340(h). Subsection (b) requires the filing of valuation reports similar to the requirement in present Section 21.84.350, but the valuation standards are set forth in MFC Section 21.84.1250. Subsection (c) provides a penalty for late filing of an annual statement, the same as in present Section 21.84.360.

21.84.1270      21.84.030      Annual License - is essentially the same as present law.

21.84.1280      21.84.370; .380; .390

Examination of Societies; No Adverse Publications - This section covers both domestic, foreign and alien societies. The confidentiality requirement of present Section 21.84.390 is preserved. Insurance Department examination of fraternal would be on the same basis as for commercial life and health insurers.

21.84.1290	21.84.040	Foreign or Alien society - Admission - Is essentially the same as present law.
21.84.1300	21.84.530	Injunction - Liquidation - Receivership of Domestic Society - This section is essentially the same as present law.
21.84.1310	21.84.050	Suspension, Revocation or Refusal of License of Foreign or Alien Society - is substantially the same as present law.
21.84.1320	21.84.540	Injunction - This section provides that only the Director of Insurance may bring an injunction proceeding against a society, not private litigants.
21.84.1330	21.84.590(7); AS 21-27	

Licensing of Agents - Subsection (a) provides that full-time fraternal agents will be required to meet the same licensing and regulatory standards applicable to commercial life insurance agents under AS 21.27, the same as present law. AS 21.27.060(d)(1) provides that an applicant for a limited license under AS 21.27.150(5) [a fraternal benefit society limited producer license to a person whose sole purpose is to be appointed by and to act on behalf of a fraternal benefit society] shall not be required to take an examination.

Subsection (b) provides that no examination or license shall be required of salaried persons who devote substantially all of their services to other than solicitation of insurance and who receive no commission or compensation dependent upon the amount of business obtained.

Subsection (c) provides an exemption from licensing of persons who devote only part-time to the solicitation of insurance and who in one year write no more than \$50,000 of life insurance or other insurance on a maximum number of 25 persons.

The Alaska Producers Act, AS 21.27, does not have the exemptions provided in subsections (b) and (c).

21.84.1340	21.84.470; .480; .590(9); AS 26-36	
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Unfair Methods of Competition - This section makes it clear that fraternal organizations are subject to the unfair trade practices and frauds laws of Alaska contained in AS 26-36, the same as provided in present Section 21.84.590(9). This section also makes it clear that unfair trade practices laws are not to be interpreted to interfere with membership practices of fraternal organizations. The application of AS 26-36 to fraternal organizations makes obsolete and unnecessary retention of the text of present Sections 21.84.470 and 21.84.480.

21.84.1350	21.84.490	Service of Process - Is essentially the same as present law.
21.84.1360	(None)	Penalties - This section provides specific penalties for certain violations in addition to the penalties specified in other sections. Subsection (a) contains the penalty for misrepresentation in present Section 21.84.470(b). Subsection (d) is a general catch-all penalty for a violation for which a specific penalty is not provided.
21.84.1370	21.84.550	Review - is essentially the same as present law.
21.84.1380	21.84.020	Exemption of Certain Societies -- Is the same as present law. The words "health care" are used in subsections (a)(3), (a)(4), (b) and (d) to reflect the amendments enacted by sections 98, 99 and 100 of S. 319, Laws of 1996.
21.84.1390	(None)	Severability - This section creates a rule of construction for courts ruling on a provision or provisions of this chapter that may not affect other sections.

D. Why not further amend the existing Chapter 84 rather than enact a whole new fraternal code?

A review of the changes made by the NFCA 1983 Model Fraternal Code indicates that the improvements are so numerous that a piecemeal amendment process to Chapter 84, as has been done frequently in the past, would not produce the same effect.

Uniformity of regulations is important to multi-state operations. When a statute on a certain subject is different than the one in another state, it makes varying interpretations more likely. That produces the need for different forms, different member benefits, complicated operations, and frustrated management.

What amendments would be given what priority? How many times would amendments be needed? This new Code provides a means to keep pace with things without constantly seeking law changes. Also, the Model Code would be a more readily understandable statute than present law, and would give the Alaska Director of Insurance more regulatory authority over fraternal benefit societies than does present law.

The NFCA Model Fraternal Code is the product of professional deliberation and scholarship which accounted for all aspects of fraternal operations. Its enactment in Alaska would produce far better legislation than could piece-meal amendments to solve a problem here and a problem there.

#### E. Summary.

Enactment of the MFC in Alaska would in no way affect the rights of existing society members and certificate holders.

The MFC would, though, affect the future conduct of business of fraternal societies in Alaska. The MFC gives societies certain additional authority under Sections 21.84.1050, .160(a)(7) and .220(c). The MFC would also strengthen regulatory control over societies by the Insurance Director: particularly, (1) under Section 21.84.1100 by increasing the organizational financial requirements for new societies; (2) under Section 21.84.1190 (f), requiring that all new certificates filed after one year from the effective date of the code shall conform to the same policy requirements as established for the same kinds of policies issued by commercial life and health insurers; and (3) under Sections 21.84.1200 and 21.84.1250, requiring the calculation of nonforfeiture benefits and the valuation of certificate reserves on new business on at least the 1941 CSO Table of Mortality.

The provision of MFC Section 21.84.1160(a)(7) that a fraternal benefit society may provide such other benefits as authorized for life and health insurers (which are not inconsistent with the concepts and fundamental nature of fraternal as expressed in the MFC) should be a major benefit to present members and future members of societies. Under that provision, the Director of Insurance can approve new forms of insurance for fraternal that have likewise been approved for commercial life and health insurers, without having to wait for the Legislature to enact an otherwise necessary amendment to the fraternal chapter.

MFC Section 21.84.1170(a) authorizes a society to provide that the owner of a benefit contract may designate an irrevocable beneficiary, and Section 21.84.1190(h) would authorize assignment of a benefit contract to a third party.

In summary, it is believed that the MFC would provide a clearer and more comprehensive statute regulating fraternal benefit societies than present Chapter 84 and would give the Director of Insurance more authority and control over their operations. The MFC provisions would be more beneficial and provide more protection to the people in Alaska who are or may choose to become members of and insured by a fraternal

benefit society licensed in Alaska. In addition, several sections clarify the law by specifically providing for the particular regulatory authority under Chapter 84, with particular references to other applicable chapters and sections.

There are no domestic fraternal benefit societies in Alaska of which we are aware, but there are six member-societies of the National Fraternal Congress of America from other states licensed in Alaska.

These societies have nearly 7,600 life insurance certificates and over 280 health insurance certificates on their members residing in Alaska. It is desirable that these societies be able to offer to their members in Alaska the benefits afforded by this new Model Fraternal Code.

Therefore, on their behalf the NFCA urges the introduction and enactment of the Model Fraternal Code bill in the 1997 session of the Alaska Legislature.

A legislative bill draft in the Alaska format and style is submitted with this Proposal.

Attached are two cross-reference charts showing corresponding sections of the Model Fraternal Code bill with the sections in present Chapter 84, and vice versa.

Respectfully submitted,

National Fraternal Congress of America  
1280 Iroquois Drive, Suite 300  
P.O. Box 3087  
Naperville, Illinois 60566-7087  
(630) 355-6633  
October 1996

# Fax Transmittal Cover Sheet

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To: Shirley Armstrong, - House L&C Committee

From: Charlie Miller

Fax Number: 586-1476

Date: Mon, Mar 10, 1997 • 2:39 PM

Pages, including cover: 2

If there is difficulty with this transmission, please call: 463-5062

Note:

Here is the list from a Division of Insurance report on the fraternal organizations licensed in the State of Alaska.

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**1994 LIFE, ANNUITY AND A AND H  
BUSINESS FOR FRATERNAL ORGANIZATIONS  
(\$000)**

COMPANY NAME	DOM	LIFE				A & H PREMIUMS		
		ISSUED DURING CURRENT YEAR	IN FORCE END OF YEAR	PREMIUMS WRITTEN	BENEFITS PAID	ANNUITY CONSIDERATIONS	COLLECTIVELY RENEWABLE	ALL OTHER
AID ASSOCIATION FOR LUTHERANS	WI	17,861	190,841	1,140	725	1,039	0	150
AMERICAN POSTAL WORKERS ACC BNFT ASN	NH	0	0	0	0	0	0	0
INDEPENDENT ORDER OF FORESTERS US BR	NY	555	42,113	358	195	5	0	1
KNIGHTS OF COLUMBUS	CT	17	2,679	20	27	0	0	2
LUTHERAN BROTHERHOOD	MN	15,016	134,390	947	712	203	0	129
SONS OF NORWAY	MN	1,748	23,406	288	1,271	339	0	2
WOODMEN OF THE WORLD LIFE INS SOC	NE	0	941	10	28	0	0	0
<b>TOTAL</b>		<b>35,197</b>	<b>394,370</b>	<b>2,759</b>	<b>2,956</b>	<b>1,586</b>	<b>0</b>	<b>284</b>

7 COMPANIES

**RECAP OF 1994 ALASKA ACCIDENT & HEALTH BUSINESS\*  
(LIFE, AND PROPERTY & CASUALTY INSURERS - \$000)**

	DIRECT WRITTEN PREMIUMS	DIRECT EARNED PREMIUMS	DIRECT LOSSES INCURRED
GROUP	249,670	197,668	158,812
CREDIT	4,628	4,525	2,437
COLLECTIVELY RENEWABLE	277	284	16
ALL OTHER	10,124	10,372	5,074
<b>TOTAL</b>	<b>264,699</b>	<b>212,849</b>	<b>166,339</b>

\*Includes Canadian Life Insurers

MAR 11 1997

**WOODMEN OF THE WORLD/OMAHA WOODMEN  
LIFE INSURANCE SOCIETY**



WOODMEN TOWER, 1700 FARNAM ST.  
OMAHA, NEBRASKA 68102  
TELEPHONE (402) 342-1000  
FACSIMILE (402) 841-0656

March 11, 1997

VIA FACSIMILE 907-465-2040

The Honorable Norman Rokeberg  
Alaska State House of Representatives  
Juneau, Alaska

**MARK D. THEISEN**  
*Vice President and  
General Counsel*

**CALVIN E. ROBINSON**  
*Vice President and  
Associate General Counsel*

**JAMES M. GLEASON**  
*Assistant Vice President and  
Associate General Counsel*

**LYNN L. ESPELAND**  
*Assistant General Counsel*

**S. JAMES PATTERSON**  
*Assistant General Counsel*

Dear Representative Rokeberg:

Re: H.179 (Model Fraternal Code)

On behalf of our 117 members in the State of Alaska, Woodmen of the World/Omaha Woodmen Life Insurance Society strongly supports the adoption of the Model Fraternal Code in Alaska. We hope that Alaska will join the over two-thirds of other states who have adopted the Model Code on behalf of fraternal benefit societies and fraternalists in their states.

Again, we support H.179 and concur with statements made in support of H.179 by the individual who will be representing the National Fraternal Congress of America (NFCA), who I believe will be Mr. Rick Kleven of Lutheran Brotherhood.

Sincerely,

Mark D. Theisen  
Vice President and  
General Counsel

lj

cc: David J. Brummond, General Counsel  
National Fraternal Congress of America



**H. Wayne Berg**  
District Representative

P.O. Box 3247  
Ketchikan, AK 99901  
Phone: (907) 225-8965

March 10, 1997

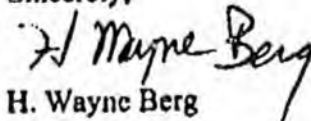
Representative Norman Rokeberg  
Chairman, House Labor and Commerce Committee  
Alaska State Legislature

Dear Mr. Chairman;

I am writing to indicate my support of H.F. 179 and S.F. 119, which would bring the Model Fraternal code to Alaska. As a fraternalist, member of and District Representative for Lutheran Brotherhood, this bill is important to me as it will allow fraternalists the flexibility to meet the needs of their members now and in the future. It will not change our basic nature as not-for-profit, self-help membership organizations, with local lodges throughout our state and the rest of the nation.

Thank you for your support of this bill.

Sincerely,



H. Wayne Berg  
600 Main St.  
Ketchikan, Ak. 99901