A Comparative Analysis of Bank Security in A Letter of Credit Transactions: The Pledge of a Bill of Lading under English and Ethiopian Law

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Abstract

This article examines the security of banks using bills of lading as collateral in letter of credit transactions with a focus on proprietary and contractual rights. The exploration employs doctrinal tools of comparative analysis. Juxtaposing the features of English and Ethiopian laws, the investigation unraveled issues, such as proprietary and contractual rights, banks' ability to claim delivery or sue carriers, and the legal consequences of these issues. The evidences from the comparative analysis show that the English law clearly sanctions prejudicial legal consequences on banks whereas the Ethiopian law leaves outcomes ambiguous. Further, the exploration reveals that the validity of security interest may be challenged if goods are delivered before the bill reaches the bank. Yet this is treated as spent under Ethiopian law, in contrast to the case law under English law. Both jurisdictions require the transferor to hold title, potentially invalidating the bank's security if the seller lacks title. Besides, the English law considers the intention of parties in transferring title via bills, while Ethiopian law lack such clarity. The financing bank's temporary release of the bill of lading in return for trust receipts further undermines its security under both legal systems. Finally, pledging bills of lading as collateral may leave banks as unsecured creditors, questioning the perceived reliability of this security mechanism.

Key Words: Letter of Credit, Bank Security, pledge, Bill of Lading, Document of Title, Misdelivery Action

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Introduction

Letter of credit transaction is one of the key elements of international business interactions in which a buyer and a seller belong to different jurisdictions. In such transactions, a seller is generally unwilling to ship goods without first ensuring receipt of payment, while the buyer is similarly hesitant to pay without adequate assurance of receiving the goods.[1] A letter of credit, which makes banks a central actor, tries to strike a balance between these opposing interests.[2] Upon the buyer's request, a bank, which is more creditworthy than the buyer, will promise the seller that it will pay the contract price once documents evidencing shipment are presented. On the other hand, the buyer is only supposed to pay upon the arrival of a complying document in the hands of the bank, evidencing that the goods have been shipped as agreed.

By financing the sale contract, the bank is essentially assuming accountability for failure of the buyer to reimburse the sale price that it advances to the seller.[3] As such, its willingness to absorb the buyer's bankruptcy, for instance, is dependent on the strength of the securities that the letter of credit offers.[4] In the failure of the buyer, the bank can resort to these securities. In fact, financing banks can ask other alternative securities, such as requiring the buyer to present other collaterals; however, practically, a transferable bill of lading is

[1] Carole Murray, David Holloway and Daren Timson-Hunt, *The Law and Practice of International Trade* (13thedn, 2019) 11-001; See also, Charles Debattista, *The Sale of Goods Carried by Sea* (2nd ed, Butterworths 1998) pp. 1-14.
[2] Časlav Pejović, *Transport Documents in Carriage of Goods by Sea: International Law and Practice* (1st ed, Informa Law from Routledge 2020) p. 163.
[3] HC Gutteridge and Maurice Megrah, *The Law of Bankers' Commercial Credits* (7thed, Europa Publications Limited 1984) p. 210.
[4] Torsten Schmitz, 'The Bill of Lading as a Document of Title' (2011) 10 Journal of International Trade Law and Policy 255.

preferable. By holding the bill of lading by way of pledge, the financing bank can establish title to the underlying goods.

In an international carriage of goods by sea, a bill of lading is a document that functions as a receipt of goods, evidence of a carriage contract and a document of title to goods.[5] Its function as a "document of title" makes it an ideal option for banks to acquire security interests on the underlying goods. Its document of title function implies that a bill of lading serves as the symbol of the goods described in it, so its transfer can pass the constructive possession of the goods.[6] Further, though it does not by itself transfer title to goods, it can be part of the process of transferring title depending on the intention of parties to the sale contract.[7]

Revisiting the issue of bank security in a letter of credit and the financing bank's willingness to absorb risks associated with the potential bankruptcy of the buyer before being reimbursed for its payments depends on the security that the bill of lading provides. To that end, the bank may subject the goods described by the bill of lading as collateral by holding the bill of lading as pledge. The bank, as pledgee of the bill of lading, will have a special property on the underlying goods.[8] This gives the bank a power of sale and a priority

[5] Sir Guenter Treitel and FMB Reynolds, *Carver on Bills of Lading* (1st edn, Sweet & Maxwell 2001) paras 1-3; See also, Frank Stevens, *The Bill of Lading Holder Rights and Liabilities* (Routledge 2018) p. 1.

[6] Enichem Anic Spa v Ampelos Shipping Co Ltd (The Delfini) [1990] CA 1 Lloyd's Rep 252; Michael D Bools, *The Bill of Lading: A Document of Title to Goods an Anglo-American Comparison* (LLP Limited 1997) pp. 1-18.

[7] The Delfini (n 6).

[8] Paul Todd, *Bills of Lading and Bankers' Documentary Credits* (4th ed, Informa 2007) 6.19.

right in the proceeds of the sale of the underlying goods, in case the buyer becomes bankrupt before reimbursing the bank.[9]

Further, from a contractual rights perspective, the bank can also claim delivery of the cargo from the carrier upon the arrival of the goods at the port of destination if its client fails to reimburse the amount paid to the seller. Moreover, if the carrier has already delivered the cargo to a third party without the production of the bill of lading, the law entitles the bank to institute a "misdelivery action" against the carrier.[10] Finally, it important to note that a bill of lading as collateral for financing banks is not as robust as commonly perceived, as several variables limit its reliability.

This article aims to identify these factors and evaluate the strength of a bill of lading as collateral under English and Ethiopian law from a comparative perspective. The study employs doctrinal legal research methodology to analyze and interpret primary and secondary legal sources. By using statutory provisions, case law, and legal doctrines as target of juxtaposition, this method allows for a structured comparison of how English and Ethiopian laws treat the pledge of a bill of lading. The English law is chosen for comparison due to its well-established legal framework governing international trade and maritime commerce, its influence on global commercial law, and its extensive jurisprudence on the bill of lading, making it an ideal benchmark for comparative analysis.

[9] Edward Ivamy, Payne and Ivay`s, *Carriage of Goods by Sea* (Butterworths, London, 13thed, 1989) p. 72.

[10] The COGSA 1992, Art 2. A misdelivery action against a carrier arises when a carrier delivers goods to the wrong party or fails to deliver them according to the terms of the bill of lading or shipping contract. This action typically involves a claim by the party entitled to receive the goods (often the consignee or the holder of the bill of lading) against the carrier for breaching the delivery terms.

1. Overview of Pledging a Bill of Lading under English Law

1.1. The Nature of Bill of Lading as Document of Title

The function of a bill of lading as document of title has two implications. Firstly, a bill of lading designates goods under voyage. This makes the instrument a transferable key to the warehouse, allowing transfer of constructive possession of goods. Second, it is essential in transferring title to property. While its transfer alone cannot transfer title to goods, it remains a crucial part of the process. Thus, the document of title function of a bill of lading makes it a pledgeable asset.

Under English law, only the intention of parties to a sale contract can transfer property, not the transfer of a bill of lading.[11] If the intention to transfer property accompanies the transfer of a bill of lading, then the transfer of the bill of lading can effectively transfer the property. Thus, a bill of lading, being a document of title, does not necessarily indicate that the holder has title to the goods.

Under English law, for a bill of lading to serve its document of title function, it must be capable of transferring rights and liabilities. Section 1 (2) (a) of COGSA 1992 suggests that a bill of lading is said to be transferable only when it can transfer title either by delivery alone or endorsement followed by delivery. This implies that only bills of lading issued either in bearer or order form can be considered transferable and serve as a document of title.

[11] Sale of Goods Act 1979 (The Sale of Goods Act), s .17.

1.1. The Pledge of a Bill of Lading in a Letter of Credit Transaction

As a document of title, a party holding a bill of lading, which may also be the bank financing a sale contract, can acquire constructive possession of the goods under voyage. As a result, only this party has a contractual right to demand delivery of the cargo from the carrier or to take legal action if the carrier delivers the cargo to the wrong party.[12]

In this context, the bank's rights to claim delivery of the cargo or sue the carrier are only contractual rights available to it, like any other holder of a bill of lading. These contractual rights of the Bank come from its position as a consignee, endorsee, or bearer holder under Section 5(2) of COGSA 1992, not necessarily from being a pledgee of the bill of lading.

However, banks often choose to obtain title to the goods by taking the bill of lading as a pledge instead of exercising contractual rights, as this may require them to join the carriage contract and incur related costs.[13] This is because pledging the bill of lading subjects the underlying goods to the pledge, securing the bank's right to be reimbursed by its client, the buyer. This grants them the power of sale of the goods and priority in the proceeds of the sale. Besides, by obtaining title under the documents, banks can also realize their claim against their client by reselling the document.

Pledge is generally one of the possessory types of security interests under English law. Its possessory nature implies that the subject matter

[12] The COGSA 1992, s 5 (2).

[13] The COGSA 1992, s 3(1); See also, section 3.1 of this article about how the exercising of contractual rights might be a reason for the bank to be liable to different costs as if it is a party to the carriage contract.

of a pledge is only corporeal assets and documentary intangibles.[14] Because it is possessory, it will affect third parties only when the pledgee is in possession of the pledged asset.

Holding the bill of lading satisfies the possession requirement of a pledge, as it provides constructive possession of goods in transit until they reach the destination port.[15] However, this possessory requirement is not absolute. In certain circumstances, the bank may temporarily release the pledged bill of lading without relinquishing its rights as the pledgee. For instance, if the buyer is unable to pay the bank and take possession of the bill of lading, but the goods have already arrived at the port of destination, the bank might release the bill of lading to enable the buyer to receive the cargo from the carrier. In these situations, the bank may issue a trust receipt, enabling the buyer to obtain the cargo from the carrier while also demonstrating that the buyer holds the bill and the underlying goods on behalf of the bank.

[14] Goode RM, *Legal Problems of Credit and Security* (2nd ed, Sweet and Maxwell Ltd 1988) 11. Documentary intangibles are documents embodying title to goods, money, or securities such that the right to these assets is vested in the holder of the document for the time being and can be transferred by delivery with any necessary endorsement.

[15] *Official Assignee of Madras v Mercantile Bank of India Ltd* [1935] AC 53.

1. Overview of Pledging a Bill of Lading under Ethiopian Law

1.1. Understanding the Nature of a Bill of Lading under Ethiopian Law

The Commercial Code recognizes bill of lading as a negotiable instrument. Book IV of the Ethiopian commercial code regulates a negotiable instrument, which include commercial instruments[16], documents of title to goods, and transferrable securities.[17] Particularly, title I of book IV, in Articles 715 - 731, provides the general provisions applicable to all the three types of negotiable instruments. Except these general provisions, the code has no specific provisions governing documents of title to goods and what it calls transferable securities. The specific provisions of the code are limited to commercial instruments such as cheque, bill of exchange and promissory note.

As bill of lading is one of the most widely recognized documents of title to goods, the term 'documents of title to goods' under the Ethiopian commercial code encompasses a bill of lading.[18] One can therefore assert that the general rules of the Ethiopian commercial code mentioned above are applicable to a bill of lading as well. These provisions regulate the definition of a negotiable instrument, the form of issuance, its modality and effect of negotiation, and defenses.

Illustrating these evidences, Article 715(1) of the code, defines negotiable instrument I as "a document that incorporates a right of entitlement such that the rights cannot be enforced or transferred

[16] Commercial instruments are negotiable instruments incorporating the right to receive money such as cheques, bills of exchange, and promissory notes.

[17] The Ethiopian Commercial Code, Art 715(2).

[18] A bill of lading is one of the most widely recognized documents of title to goods, but other documents, such as warehouse receipts and dock warrants, also serve similar functions in different commercial contexts

independently of the document." This provision highlights two elements essential for understanding the document of title function of a bill of lading: the right of entitlement and the inseparability doctrine.

The notion of right of entitlement signifies that a negotiable instrument incorporates a right: the right to receive goods or a sum of money. In the context of a bill of lading, the right associated with it is the right to receive goods. Besides, the element of inseparability indicates that the rights associated with a negotiable instrument can only be transferred or enforced when accompanied by the document itself. This inseparability ensures that the document and the embodied rights are inextricably linked. In the context of a bill of lading, the holder has the right to receive the underlying goods from the carrier, but this right can only be exercised upon the presentation of the bill. The carrier can refuse anyone claiming the cargo without the bill of lading at hand. Further, to transfer the title to goods, one must also transfer the bill of lading.

The Movable Property Security Rights Proclamation (hereinafter the Security Rights Proclamation) also recognizes a bill of lading as a corporeal movable property. Generally, the Proclamation designates movable property as the sole object of security rights, further classifying it into corporeal and incorporeal categories. Within this framework, a bill of lading is categorized as corporeal movable property even though the right it bears is incorporeal.

One of the key elements, taken as new practices introduced in this Proclamation is its distinct approach to classifying documentary intangibles.[19] Unlike the traditional classification found in the

[19] A documentary intangible is a physical document that embodies an incorporeal right, meaning the document itself represents a legal claim rather than having intrinsic value. It serves as evidence of a right that can be transferred by transferring

Commercial Code, which broadly groups all documents entitling the holder to receive either money or goods under the term negotiable instruments, the Proclamation draws a distinction between negotiable instruments and negotiable documents.

Under the Commercial Code, consistent with the approach of many civil law legal systems, the term negotiable instrument applies to various documents incorporating rights to receive either money or goods. However, the Security Rights Proclamation adopts a narrower definition, limiting negotiable instruments to documents that strictly confer the right to receive money. This category includes instruments such as promissory notes, checks, and bills of exchange.

Simultaneously, the Proclamation introduces the term negotiable document to refer specifically to documents that entitle the holder to receive goods. This newly defined category includes bills of lading and warehouse receipts—documents that represent claims to goods rather than monetary payments. By drawing this distinction, the Proclamation provides a more structured classification, clearly separating financial claims from claims to goods.

The Proclamation appears to have intended to adopt the approach taken by the Uniform Commercial Code (UCC) of the United States, which distinguishes between negotiable instruments (Article 3) and documents of title (Article 7). Nevertheless, it is also somewhat different because it uses the term negotiable document for those documents that entitle the holder to receive goods, while the UCC refers to these as documents of title. This choice of terminology appears confusing as a negotiable

the document, making it distinct from purely intangible assets like intellectual property.

document could be any document incorporating rights be it the right to receive money or goods.

In a related context, the nature of the title a bill of lading represents is an issue that Ethiopian law does not seem to address. Until the 1992 Carriage of Goods by Sea Act resolved many interpretational dilemmas, the English law had also similar problems. Central to this discussion is whether the holder of a bill of lading is the owner of the goods or merely entitled to demand delivery. This also raises questions over the transferability of rights, such as whether the holder can pass ownership or entitlement to others by endorsing the document, and whether the holder can sue the carrier for damage to the cargo during transit. The way these issues are addressed determines how the bill of lading functions: whether it merely serves as a receipt and contract of carriage or confers proprietary rights.

In conclusion, the combined elements of the right of entitlement and inseparability under the commercial code, along with the possibility of subjecting a bill of lading to security rights in the security proclamation, make it possible to argue that a bill of lading is a document of title to goods, and its transfer can indeed transfer constructive possession of goods. However, while it provides a foundational understanding of negotiable instruments, which include a bill of lading, the commercial code lacks provisions addressing the unique features of bills of lading. Most importantly, key aspects regarding the nature of a bill of lading, such as identifying the holder of a bill of lading and the extent of rights, are left unaddressed. Recourse to the Maritime Code itself gives no better outcome. The maritime code governs a bill of lading in Articles 180-209, focusing only on its role as a contract of carriage. The role of a bill of lading as a document of title is unaddressed.

It was anticipated that the upcoming Financial Services Code would address the issues of ambiguity and gaps in the law governing negotiable instruments, including bills of lading. However, according to the code's drafters, its original provisions will largely remain unchanged, except for cheques, which will undergo significant legislative reforms.[20]

2.2 Security Rights[21] on a Bill of Lading in a Letter of Credit Transaction under Ethiopian Law

2.2.2 Pledging Endorsement under the Commercial Code: Real Security or Legal Fiction?

Security is the other subject requiring close scrutiny in Ethiopian commercial practices. Looking into both the Maritime Code and Commercial Code, one would see that both are not clear as to whether if financing banks in a letter of credit transaction can hold a bill of lading by way of security. Of course, one may argue that Article 729 of the Commercial Code allows negotiable instruments to be subjected to security through endorsement. However, this provision presents challenges if we interpret it as also allowing financing banks to hold a bill of lading by pledge.

[20] The Core Drafting Team, The Reform of the Banking Law of Ethiopia: Defining the Scope of the Reform (Policy White Paper, Ministry of Justice of the Federal Democratic Republic of Ethiopia, August 2022) 16 (unpublished, on file with the author). In addition to the white paper, the author personally consulted one of the drafters, who confirmed the same position regarding the scope of the reform. This direct confirmation supports the accuracy of the cited document and its conclusions.

[21] The writer intentionally used "security rights" in the context of bills of lading in Ethiopia, whereas English law refers to it as "pledge." This choice aligns with the approach taken by Ethiopian law. In Ethiopia, the Security Rights Proclamation adopts a universal approach to security rights, meaning it does not categorize security devices into specific types like pledge or mortgage. Instead, the law establishes a comprehensive security rights framework, regardless of the terminology used by the parties. Consequently, banks in Ethiopia establish security rights over a bill of lading, not pledge.

The issue is that an endorsement by way of pledge, under Article 729 of the commercial code, reduces the endorsee to an agent, not a principal acting independently. An endorsee, when acting as a pledgee, has restricted rights. Specifically, it cannot transfer full title to the underlying goods and is limited to transferring its security interests, like the abilities of an agent. However, in a letter of credit transaction, issuing banks mostly prefer to transfer the bill of lading to third parties to realize their claims in their capacity independently.

Thus, from this evidences one could see that, under Article 729, financing banks are relegated to mere agents, which hampers their ability to transfer rights and realize claims. Endorsement for pledge is not therefore a genuine security mechanism. True security rights should empower the holder not only to exercise the rights incorporated in the instrument but also to transfer those rights fully and independently.

1.1.1. Security Rights on Bills of Lading: The Approach of the Security Rights Proclamation

Unlike the commercial code, the Security Rights Proclamation explicitly allows for the possibility of establishing a full-fledged security right on a bill of lading. The Proclamation is generally the first comprehensive law to regulate the creation and enforcement of security rights in Ethiopia. It provides a platform for creating security rights on movable properties.

It adopts a unitary concept of security rights, abolishing the 1960 Ethiopian Civil Code’s fragmented concept of security rights.[22] It does not specifically mention a particular type of security device such as

[22] Asress Adimi Gikay, *Ethiopian Law of Security Rights in Movable Property* (2021) pp. 46-48.

pledge, charge, or retention of title. It instead governs any transaction that aims to secure payment or the performance of contractual obligations, irrespective of the name parties ascribe.[23]

Under English law, a security right on a bill of lading takes the form of pledge, which is possessory as a principle.[24] However, in Ethiopia, whether parties call it a pledge, a security interest is created once all necessary conditions are met. Although the proclamation establishes non-possessory security as the principle, negotiable instruments are an exception since their perfection requires possession alone. The transfer of possession of the document is necessary for the security interest to be enforceable against third parties.[25]

Article 4 of the proclamation provides the modes of creating security rights. It prescribes that a security right must be created by a separate agreement. However, when it comes to a bill of lading, a security agreement alone is not enough for a bank to create security rights on a bill of lading. Unless the bank is mentioned in some capacity, such as an endorsee or consignee, it cannot claim delivery of the goods from the carrier, nor can it transfer its rights to third parties to realize its claims. Besides, it has no right to sue the carrier in cases of misdelivery or damage to the cargo, for which the carrier is responsible.

[23] Asress Adimi Gikay, 'Rethinking Ethiopian Secured Transactions Law through Comparative Perspective: Lessons from the Uniform Commercial Code of the US' (2017)11 Mizan Law Review 154. Article 3(1) stipulates that 'This proclamation shall apply to rights in movable property created by agreement that secure payment of credit or other performance of an obligation.'

[24] Possessory security is a type of security interest where the creditor takes physical possession of the debtor's asset as collateral for a loan. Common examples include pledges and liens, where the creditor holds the asset until the debt is repaid.

[25] The Security Rights Proclamation, Art 13 (2).

This limitation arises from the inseparability of the rights from the document in a negotiable instrument. Anyone wishing to enforce or transfer the rights incorporated in a negotiable instrument must present the document. Therefore, without being explicitly named in the capacity of endorsee or consignee, the bank's ability to exercise or transfer these rights is severely restricted. In essence, unless the bank is named in the bill of lading, it is left with an unenforceable power of sale in the security agreement, effectively rendering the agreement an empty shell.

In conclusion, the method of creating security rights in the proclamation does not adequately consider the unique characteristics of a bill of lading specifically and negotiable instruments in general.

2. Issues Surrounding Rights over Bill of Lading as a Security under English and Ethiopian Law

A bank financing a sale contract on behalf of a buyer may hold the bill of lading, which comes into its possession upon the seller presenting documents for payment, as a pledge. This grants the bank control over the cargo and, importantly, establishes title to the goods, serving as security against the possibility of the buyer becoming insolvent before reimbursing the bank.

From a contractual rights perspective, the pledge of the bill of lading entitles the financing bank to claim delivery of the cargo from the carrier or to institute a misdelivery action against the carrier if the goods are delivered to third parties without a bill of lading. From a proprietary rights perspective, on the other hand, the bank acquires special property in the underlying goods, granting it the power of sale and priority over the proceeds of the sale in the event of the buyer's bankruptcy.

However, there are issues that could potentially compromise the strength of a bill of lading as collateral for financing banks. The purpose of this section is therefore to critically appraise the strength of pledging a bill of lading in securing the reimbursement rights of the financing bank in a letter of credit transaction, considering English law and Ethiopian law from a comparative perspective.

In evaluating its strength, the next sections article addresses the conditions under which the bank may join the contract of carriage and its implication for bank security, the discharge of the underlying goods by the carrier before the transfer of the bill of lading to the bank, the transfer of title to the buyer before the seller transfers the bill of lading to the bank, the absence of intention to transfer possession on the part of the seller upon transferring the bill of lading, and the risks consequent to the bank's temporary release of the bill of lading in return for a trust receipt.

3.1. The Role of Contractual Security Mechanisms

Under English law, as mentioned in earlier sections, a financing bank that holds a bill of lading by way of pledge has two sets of contractual rights against the carrier - the right to claim delivery of the cargo and the right to bring a misdelivery action.

The first right is straight forward directly derived from the nature of a bill of lading as a document of title entitling the bank the constructive possession of the goods all the way through the voyage. However, the second one, the right to suit is explicitly provided in COGSA 1992. This right entitles the bank to institute an action for compensation against the carrier for misdelivery or damage to the cargo for reasons the carrier is liable. This Act made the right of suit available for every lawful holder of a bill of lading. Section 2(1) (a) of the Act provides that 'a person who becomes the lawful holder of a bill of lading shall …be vested in him all rights of suit under the contract of carriage.'

Nevertheless, the bank's exercise of any of the above contractual rights may end up with the bank joining the carriage contract to which it is less interested. Under COGSA 1992, a lawful holder of a bill of lading joins the carriage contract with all the consequences attached when it claims to enforce its rights. If the bank wishes to enforce its contractual rights against the carrier, under section 2(1) (a), it will be liable 'under the carriage contract as if he had been a party to that contract.' Section 3(1) further clarifies what it means by a 'claim to enforce contractual rights' that the lawful holder of a bill of lading may be held liable as a party to the contract of carriage if it either takes or demands delivery of any of the goods from the carrier or makes a claim under the contract of carriage against the carrier in respect of any of those goods.

Of course, section 3(1) of COGSA1992 is commendable for resolving the problem that financing banks falls under the 1855 Bills of Lading Act, which made banks liable under the carriage contract merely because they were mentioned as a consignee, endorsee or were in possession of a bearer instrument.[26] Under COGSA 1992; however, banks will not join the carriage contract and take contractual liabilities until they take some positive steps to enforce their rights. The bank will be a party to the carriage contract and be required to assume certain liabilities to the carrier, such as unpaid freight, demurrage, storage costs, and undeclared dangerous goods, only if it claims delivery from the carrier or brings a misdelivery action.[27]

Consequently, from the perspective of the bank's security, Section 3(1) of COGSA 1992 made the bank's contractual rights less enforceable because it treats banks as parties to the carriage contract if they choose

[26] Shane Nossal, 'Revision of the Legislation Relating to Bills of Lading and other Shipping Documents' (1993) 23 Hong Kong Law Journal 115.

[27] Kourosh Majdzadeh Khandani, 'Rights and Liabilities of the Consignees/Endorsees: A Comparative Study of the Rotterdam Rules and English Law' (PhD Thesis, The University of Manchester 2018) 100-103; When a bank becomes a party to the carriage contract by claiming delivery of goods or initiating a misdelivery action, it assumes specific liabilities to the carrier, including unpaid freight, demurrage, storage costs, and undeclared dangerous goods penalties. Unpaid freight represents the cost of transportation that the buyer has not yet settled. Demurrage charges accrue if the goods are not unloaded from the vessel within the agreed time, compensating the carrier for delays. Furthermore, storage costs are incurred if the cargo remains at the port or warehouse beyond the allotted free time. Additionally, if the goods are classified as dangerous and were not properly declared, the carrier may impose fines and additional handling fees to cover the risks and compliance costs associated with transporting hazardous materials.

to exercise such rights. This is unique in the world of pledge.[28] A pledgee normally acquires rights, not obligations, but a pledgee of a bill of lading will assume liabilities from the contract of carriage if he takes positive steps to enforce his rights.[29]

Furthermore, a bill of lading may sometimes include a merchant clause, which automatically makes every holder of a bill of lading, including financing banks, a party to the carriage contract merely by holding the document.[30] This clause further reduces the effectiveness of the bank's contractual securities by imposing additional liabilities and obligations on the bank, regardless of whether it exercises any rights under the bill of lading. As a result, the bank's position as a secured party is weakened, as it must accept the potential liabilities associated with being a contractual party to the carriage contract simply by holding the bill of lading.

Turning to the to Ethiopia legal regime, the relevant laws are silent as to when and how third parties, such as financing banks, acquire contractual rights and assume obligations in a bill of lading. The issue has been regulated neither in the Commercial Code nor in the Maritime Code, not even in the Security Rights Proclamation.

Looking into the definitions given for negotiable instruments under Article 715 of the Commercial Code and its transferability in both the Maritime Code and the Commercial Code, one would clearly see the legal basis for the document of title function of a bill of lading. From this it follows that banks have at least the right to claim delivery from the carrier if they are holding a properly constituted bill of lading. This

[28] Richard Zwitser, 'The Legal Position of the Pledgee of a Document of Title such as a Bill of Lading under Dutch Law' in Jeannie Van Wyk (ed), *Property Law under Scrutiny* (Juta and Company (Pty) Ltd 2015) p.79.

[29] *Id*., p. 79.

[30] *Id*., p. 80.

is because the right to claim delivery of the cargo is the right available to the bank as a holder of a bill of lading, which is the symbol of the goods under voyage.

A problem arises under Ethiopian laws when banks find that the carrier has already delivered the cargo or found the cargo in a damaged condition. In this case, a question arises as to whether banks in Ethiopia have the right to sue the carrier. The answer does not seem to be clear-cut. The relevant Ethiopian laws—the Commercial Code, the Maritime Code, and the Security Rights Proclamation—are silent as to whether the financing bank has a right to suit.

A reference to the general contract provisions of the civil code might be a good start to the solution. Because in Ethiopian law, if parts of any law governing special contracts are silent, the law allows for a reference to the general contract provisions.[31] Under the general contract provisions, unless parties to the carriage contract provides a stipulation to the benefit of third parties under Article 1957 of the Civil Code, banks wishing to sue the carrier may face a strong defense. The carrier may raise the defense of *privity of contract,* which is among the bedrock norms of the Ethiopian contractual framework.[32] As stated in Article 1952 of the Ethiopian Civil Code, 'contracts shall produce effects only as between the contracting parties.' As such, third parties to a contract may not derive rights or assume obligations. If the carrier raises this defense, it is unlikely that Ethiopian banks will have any viable defense before a court of law unless, as mentioned above, the carriage contract itself provides a stipulation to the benefit of third parties.

31 Civil Code of the Empire of Ethiopia 1960 (The Ethiopian Civil Code), Art 1676 (1).
32 *Id.*, Art 1952.

In conclusion, under English law the position taken by COGSA 1992 ─ that exercising contractual rights on the condition of joining the carriage contract ─ made it less attractive for financing banks to exercise contractual rights as a security. However, in Ethiopia, it remains unclear whether financing banks have a contractual right against the carrier from the outset, particularly the right to sue the carrier in the event of misdelivery or damage to the cargo. As such, it is not clear what consequences will follow if financing banks take positive steps towards exercising their contractual rights.

3.2. Discharge of the Cargo before the Transfer of the Bill of Lading to the Bank

In an international carriage of goods, there are instances where the goods are discharged long before the seller transfers the bill of lading to the financing bank.[33] If the seller presents the bill of lading after the goods have been delivered, the bill of lading would no longer serve as a document of title. Consequently, the bank does not become the pledgee of the underlying goods upon receipt of the bill of lading.[34] Without being able to subject the underlying goods to a form of security, such as a pledge, it is hardly possible to say the financing bank is a secured creditor against the buyer.

The bill traditionally operates as a key to the warehouse, evidencing possession and control over the goods described. Nevertheless, this function ceases on delivery of the goods, and hence possession of the

[33] Michael Collett KC, 'Illusory Security of Banks in Trade Finance' [2023] Butterworths Journal of International Banking and Financial Law.

[34] Liew Kai Zee and Moses Lin, 'Bills of Lading as Title and Security for Financing Banks - the Certainty of Uncertainty' (7 June 2023) <https://www.lexology.com/library/detail.aspx?g=3a2dda58-7baa-4b1f-b2cc-8486bfe6d562> accessed 7 February 2024.

bill no longer entitles the holder to the possession of the goods against the carrier as the bill of lading becomes spent.[35]

The legal effect of a spent bill of lading presents a unique challenge for a bank holding a bill of lading as a security. The issue of a spent bill of lading affects not only the contractual rights of the financing bank but also its proprietary rights. From a proprietary perspective, if the goods are discharged before the transfer of the bill of lading to the financing bank, the bank cannot be able to become a pledgee of the cargo. This is because the discharge of the cargo before the bill makes the bill of lading spent, and if the bill is spent, it loses its quality, which makes it a document of title; thus, its transfer will not entitle the holder to constructive possession of the cargo, which is an indispensable step for a bank to pledge the cargo itself.

An important question then is: when is a bill of lading considered spent, influencing its pledgeability? Under English law, there is no case law directly addressing qualifying instances where a bill of lading is said to be spent.[36] However, the widely accepted view is that mere facts that the goods were discharged when the seller tenders the transport documents will not make the bill of lading spent.[37] For instance, Section 5(3) of COGSA 1992 acknowledges the rights of a person who comes into possession of a bill of lading through a legitimate transaction, even if the timing of that transaction means the bill no longer grants the right to take delivery of the goods.

[35] Michael Collett KC (33).
[36] Paul Todd, *supra* note, 7.84.
[37] *Barclays Bank Ltd v Commissioners of Customs and Excise* [1963] 1 Lloyds's Rep.81; See also Paul Todd 7.86

Whether a bill of lading lost its quality as a document of title depends on whether the receiver who takes delivery is entitled to the goods.[38] If the person receiving the delivery cannot rightfully make such a claim of delivery under the bill of lading, the bill is not spent and thus can still transfer the title to the goods. However, if the receiver is entitled, the bill of lading will be considered spent once delivery has been made.

Who, then, is a lawfully entitled party for the purpose of a spent bill of lading? Under COGSA 1992, a lawfully entitled party can be an endorsee, the consignee of a bill of lading, or a holder of a bearer instrument.[39] The delivery of the cargo for one of these parties could make the bill of lading spent. However, this is not always the case. In the Erin Schulte[40] ─ where the underlying cargo was delivered to third parties who were not mentioned in the bill of lading as consignees nor endorsees ─ the UK Court of Appeal held, the bill of lading to be spent.

The fact show that Gunvor International B.V. sold gasoil to United Infrastructure Development Corporation (UIDC), which in turn had a contract to sell it to Cirrus Oil Services Ltd. Payment, was arranged through letters of credit, with SCB being the financing bank. Goods were shipped, and the bill of lading was issued, consigned to Société Générale or order.

Unfortunately, Cirrus and UIDC rejected the cargo on board Maria E due to issues of specification. The shipment on the Erin Schulte was also similarly rejected; however, UIDC secured third-party buyers, Chase Petroleum Ghana Limited and UBI Energy Petroleum Ghana Limited. Gunover then presented the documents on June 4, 2010, to SCB

38 AH Hudson, 'The Exhaustion of Bills of Lading' (1963) 26 The Modern Law R eview 442 <https://www.jstor.org/stable/1093218> accessed 28 May 2024.

39 Section 5 (2) a and b of COGSA 1992

40 *Standard Chartered Bank v Dorchester LNG (*The Erin Schulte*)* (Rev 1) [2014] EWCA Civ 1382.

according to the letter of credit. Despite the insistence of Gunover, the bank, SCB, rejected the documents and preferred to hold the bill of lading on behalf of Société Générale. In the middle of this disagreement, the carrier discharged the cargo to the new buyers from June 15th to June 19th, 2010, after receiving a letter of indemnity issued by the seller, Gunover.

On July 7, 2010, despite its rejection by the 4th of June, the bank, SCB, changed its position and paid the seller the total amount under the letter of credit. The bank then instituted a misdelivery action against the carrier for delivery of the cargo without a bill of lading and argued that it acquired the right to suit against the carrier, Dorchester, on the bill of lading on the 4th of June. However, the court decided that the bank had only acquired a right to the bill of lading on July 7, 2010, when it paid the seller. However, by the time SCB acquired this right, the goods had already been delivered to Chase and UBI in mid-June, making the bill of lading spent.

The implication is that even though the carrier, Dorchester, delivered the cargo to new buyers, Chase Petroleum Ghana Limited and UBI Energy Petroleum Ghana Limited, which are not lawfully titled parties in the words of Section 5(3) of COGSA 1992, the bill of lading was spent by July 7, 2010, when the bank, SCB, paid the seller, Gunover.

Looking into the Ethiopian law in this light, it appears that it is not possible to transfer contractual rights once the carrier discharges the goods indicated in a bill of lading. First, the scope of the law governing the bill of lading in the Maritime Code (Articles 180-209), is limited from the moment of loading the cargo onto a vessel to its discharge upon arrival at the port of destination. The Maritime Code, under Article 180(3), provides that it ceases to apply to issues including the status of a bill of lading once its underlying goods are discharged. This means that once the goods are delivered, the bill of lading is spent and can no longer be a document entitling the holder to exercise the rights against the carrier.

Apart from this, the Commercial Code, which recognizes a bill of lading as negotiable instrument, reinforces the position taken by the Maritime Code. Discharge is one of the real defenses available for a person sued under negotiable instrument.[41] In the bill of lading context, discharge implies the moment where the cargo is handed over to a party lawfully entitled to claim delivery. This brings the carrier's obligation under the contract of carriage to its end.

3.3. Transfer of Ownership Prior to the Transfer of Bill of Lading

The previous sub-section highlights how the discharge of the cargo before the seller tenders the bill of lading may affect the bank's ability to pledge the goods. However, there is still another factor before the bill of lading is transferred to the bank that could potentially impact the financing bank's capacity to pledge the cargo. Sometimes the seller may have already transferred title to the property for the buyer before tendering the bill to the bank.

The transfer of ownership to the buyer before the seller presents the bill of lading to the bank affects the security of the bank on the underlying goods. If title to the goods is transferred to the buyer before the seller presents the bill of lading to the bank that technically means the seller has no title, as a result he cannot create a pledge on a property to which he does not have a title. The fact that bankers normally deal only with documents but not with the underlying transactions, implies that the

[41] The Ethiopian Commercial Code, Art 717.

bank cannot refuse to accept a presentation merely because the seller has no title to the goods. This in effect makes the problem much worse.[42]

The present position under English law is that the seller must retain ownership of the cargo so that it can pledge the bill of lading to the bank financing the transaction. In the Future Express, the buyer and the seller had to delay the presentation of the document under the letter of credit.[43] Unfortunately, by the time the seller presents the documents to the financing bank, the cargo would have been delivered against the presentation of a letter of indemnity.

In cases involving such elements, both the Queen's Bench and the Court of Appeal held that the bank did not acquire pledge. In the first instance, Judge Diamond QC held that title in the goods had passed from seller to buyer long before the presentation of the bill of lading to the bank; hence, the transfer of the bill of lading did not entitle the bank to constructive possession of the underlying goods.

Furthermore, in the Court of Appeal, Judge Lloyd LJ pointed out that a seller must retain the title of the goods to be able to pledge a bill of lading. He upheld the claims of the carrier that the seller could not legally transfer the right to possession through the bill of lading as he did not have any property right over the cargo at the time of presenting the bill of lading for the financing bank. He concluded by saying that the security of the bank's position is in the capacity of the seller to transfer title upon presenting the bill on behalf of the buyer not on the contract between the bank and his client, the buyer.

[42] Uniform Customs and Practice for Documentary Credits (UCP 600) (International Chamber of Commerce Publication No 600, 2007), Art 5.
[43] The Future Express [1992] (QB) 2 Lloyd's Rep 79.

Paul Todd has also argued that 'the bank's legal title at any rate depends on the pledgor having property in the goods at the time of the pledge'.[44] That implies that the bank will acquire security by way of pledge only when the seller has retained property until it presents the bill of lading to the bank. A party who can pledge the goods is the "legal owner of the goods" and if the seller fails to retain property by the time of presenting the bill of lading to the bank, he can pass "no property to the bank as pledgee".[45]

Similarly, in Ethiopia, title is one of the conditions for creating a security agreement. Only a party with title to movable property can enter such an agreement. Evidencing this, Article 4(1) of the Security Rights Proclamation provides that 'A security agreement shall be created by a security agreement, provided that the guarantor has right in the asset to be encumbered'. Yet the English version of this sub-article fails to clarify the specific type of property right required for the guarantor to enter into a security agreement. It is not clear in the English version provision if the required title is ownership or mere possession.

In this regard, the Amharic version, which serves as a binding source of the law in cases of interpretative ambiguity, clearly defines the specific proprietary right required for the debtor to enter into a security agreement. The Amharic version says "ባለቤትነት", which is literally ownership. As a result, the debtor must have the ownership right to create a pledge over his property.

44 Paul Todd, *supra* note 14, 6.11.
45 *Id*., 6.22.

3.4. Absence of Intention to Transfer Possession with the Transfer of the Bill of Lading

The previous two sections of this article (sections 3.2 and 3.3) focused on factors that occur before the seller transfers the bill of lading to the bank. However, issues affecting the security of the financing bank are not limited to events happening before the transfer of a bill of lading; there are other factors, such as the intention of the parties to transfer title to the underlying goods during the moment of transfer. Such factors are important elements that substantially affect the party's position as a pledgee.

Under English Law whether the transfer of a bill of lading to the financing bank transfers title to the underlying cargo is dependent on the intention of the parties to the sale contract to which the financing bank can neither drive rights nor assume obligations.[46] As such, the bank could not obtain the constructive possession of the goods if parties did not intend to transfer possession of the cargo along with the transfer of the bill of lading.[47] The effect is the bank cannot acquire a pledgee status on the underlying goods if it was not the intention of parties to transfer constructive possession by the transfer of the bill of lading.

Among the instances where it was argued that the seller did not intend the transfer of a constructive possession with the transfer of the bill of lading is when the transferee (financing bank) receives the bill of lading as an agent. In a letter of credit transaction, if the seller transfers the bill of lading to the bank with the intention that the bank holds the bill as an agent, such a bank acquires only the custody of a bill of lading whereas

[46] Sale of Goods Act, S. 17.

[47] *East and West Corporation v DKBS* 1912 [2003] EWCA Civ 83.

the seller remains the possessor. In such instances, the bank will not be the pledgee of the underlying goods. [48]

In East and West Corp v DKBS, the court addressed whether a bank under such instances holds a sufficient possessory interest in goods under a bill of lading. In the Queen's Bench, Judge Thomas J noted that a bank never holds any security or interest in the goods because it holds the bill of lading as agent of the seller and the seller retains complete control over the bill of lading.[49]

Furthermore, Judge Mance LJ in this same case raised the issue of whether a transferee bank of the bill of lading vests in with a sufficient possessory interest to claim against the carrier. He held a position that property and possessory rights depend on the intention of the parties. He further cited Aliakmon where it was held that the delivery of a bill of lading to the buyer naming him as consignee did not confer possessory title since the seller did not intend to transfer such an interest.[50] He also cited Future Express where it was held that the passing of a possessory interest in common law is dependent upon the parties' intentions, emphasizing that mere physical possession of the bills of lading by the bank does not create a valid possessory title necessary to create pledge on the underlying goods.[51]

The three cases above show the position of English law that a mere transfer by the seller of the bill of lading to a bank does not confer an interest to the bank unless parties intend so. Inasmuch as the parties'

[48] Zeng Z, 'Banks' Security under Letters of Credit on Bills of Lading: Inherent Risks in Paper and Digital Contexts' (PhD Thesis, University of Southampton 2023) 88.
[49] The East West Corporation, *supra* note 47.
[50] *Ibid*.
[51] *Ibid.*

intentions matter, the bank's option to pledge the underlying goods is dependent upon the sale contract, to which the bank is not a party.[52]

In Ethiopia, the relevant laws are silent as to whether the intention to transfer title with the transfer of the bill of lading matters for the financing bank to establish security rights on a bill of lading. In this regard, Ethiopia should take lessons from the English system. In fact, the parties to the sales contract should decide when and how to transfer ownership or possession.

3.5. The Risk of Using a Trust Receipt in Exchange of Releasing the Bill of Lading

All the factors discussed so far impact the bank's security in a letter of credit transaction, but they only occur at or prior to the moment the seller transfers the bill of lading to the bank. This section focuses on a remaining factor that arises after the seller transfers the bill of lading to the financing bank— a risk consequent to the acceptance of trust receipts in return for releasing the pledged bill of lading. Such a risk happens in situations where a financing bank, as a pledgee of the bill of lading, re-delivers the bill to its customer, the buyer, in exchange for a trust receipt.

Under normal course of processes in a letter of credit transaction, the financing bank continues to hold the bill of lading as collateral until the buyer fully reimburses for the contract price paid and the commission. However, it may sometimes happen that the buyer has no assets other than the goods represented in the bill of lading, in which case the bank

[52] Richard Zwitser, *supra* note 28, p. 79.

may be forced to transfer the bill of lading to the buyer in exchange for a trust receipt.[53]

This arrangement allows the buyer to claim delivery of cargo from the carrier as he has the bill of lading. Once the buyer receives the goods from the carrier, he can sell them and retain the proceeds for the bank, thereby generating funds to settle the bank's claim for the principal debt, interest and commission.[54] Simultaneously, the bank holds the trust receipt as proof of its continued possession of the pledged item, the bill of lading, and is entitled to the proceeds of the sale of the cargo even in priority to other creditors in the insolvency of his client.[55] Therefore, using a trust receipt is beneficial not only for the bank but also for its customer, the buyer.

However, from the perspective of the financing bank's security, the use of trust receipts pose risks. Despite its obligation to hold the bill of lading and the cargo on behalf of the bank, the buyer may abuse its power by selling or pledging the bill of lading for a third party not for the bank's benefit but with intents of deriving self-interest out of this transaction.[56] Therefore, it could be very problematic for the bank, if, for instance, the buyer repledges the bill of lading to a third party as this third-party might have a better right than the bank under English law.

The Lloyds Bank Ltd. v Bank of America National Trust and Savings Association is a living testimony illuminating how the use of trust receipts in a letter of credit transaction might have a prejudicial outcome

[53] Karl T Frederick, 'The Trust Receipt as Security' (1922) 22 Columbia Law Review 395 <http://www.jstor.com/stable/1112487> accessed 3 March 2024.
[54] L Vold, 'Trust Receipt Security in Financing of Sales' (1930) 15 Cornell Law Review 543 <http://scholarship.law.cornell.edu/clr/vol15/iss4/2> accessed 30 April 2024.
[55] Zicong Zeng, *supra* note 48, p. 99.
[56] L Vold, *supra* note 54.

for the interest of financing banks.[57] The dispute in the case arose after Lloyds Bank, which financed a sale contract on behalf of Strauss & Co., released the bill of lading in its possession to Strauss & Co. in exchange for a trust receipt. Defrauding the pledgee bank, Lloyds Bank, Strauss & Co. repledged the bill of lading in its hand to the Bank of America which had no knowledge of the interest of Lloyds Bank in it. Upon the bankruptcy of Strauss & Co., the first pledgor, Lloyds Bank, claimed the delivery of the bill of lading or an award of compensation in conversion from the second pledgee, the Bank of America.

Finally, the English courts (both the High Court and the Court of Appeal) decided that the Bank of America was entitled to the underlying goods under Section 2(1) of the 1889 Factors Act. This section of the Act allows for title transfer by mercantile agents entrusted with possession of goods or documents of title. Courts considered the pledgor, Strauss & Co., as a mercantile agent for the first pledgee, Lloyds Bank, though there was no formal agent-principal relationship between them. The court held that for Section 2(1) of the Factors Act, there was no need for a formal agency-principal relationship. If it were not for the authority given by Lloyds Bank, Strauss & Co. could not have the power to dispose of the bill of lading to a third-party bank. That factual authority was enough to satisfy the requirement of "mercantile agent" under Section 2(1) of the Factors Act. This provision protects third parties who act in good faith and without notice of any lack of authority on the part of the agent.[58]

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[57] *Lloyds Bank Ltd v Bank of America National Trust and Savings Association [1938] 2 KB 14.*

[58] Louise Merrett, 'The Importance of Delivery and Possession in the Passing of Title' (2008) 67 The Cambridge Law Journal 376 <https://www.jstor.org/stable/25166410> accessed 1 April 2024; see also PT

Looking into the Ethiopian laws in this light , one could see that they would have similar result, though there have been no case laws so far. The Security Rights Proclamation governs the effect of transfers, such as the sale or repledge of an encumbered property, to third parties.

With such evidences, Article 64(2) of the proclamation provides:

> *A transferee of an encumbered negotiable document that obtains possession of the document and gives value without knowledge that the sale or other transfer is in violation of the right of the secured creditor under the security agreement, acquires its right free of a security right in the document and the corporeal assets covered thereby that is made effective against third parties.*

Like the English law, the Ethiopian provision seems to favor the third-party pledgee who is in good faith and received the pledged property for value without notice of a preexisting encumbrance. This position seems consistent with the position taken by the proclamation regarding the perfection of security rights over a negotiable document, which includes a bill of lading. Article 13(2) limits the mechanism of perfecting a security right on a negotiable document to possession only. Thus, a bank holding a bill of lading as collateral for securing its right of reimbursement should possess the bill of lading. If, for any reason, the bank releases possession of the bill of lading in favor of its client, the buyer, and then the buyer disposes of the bill of lading to third parties, the law prefers to protect the interests of third parties who are in good faith than the bank, which has willingly lost control of its collateral.

Blckwell, *The Law of Relating to Factors* (1897, Effingham Wilson, Royal Exchange London) p. 64 ff.

The only thing different in Ethiopia is the requirement of a "mercantile agent" provided under Section 2(1) of the 1889 Factors Act. In Ethiopia so long as the third-party transferee took the bill of lading by way of sale or repledge without knowledge of the previous encumbrance, it is enough to give priority to third-party than the previous pledgor. Therefore, the absence of the requirement of agency under Article 64 (2) may put financing banks in a disadvantaged position in Ethiopia compared to English law. The absence of such a requirement implies that the third party is not required to prove the fact that the pledgor was given either factual or statutory power to dispose of the property on behalf of the first pledgee.

Further, it is not clear from Ethiopian law that banks holding a bill of lading could use trust receipts as security in exchange for the release of a bill of lading to the pledgor so that it can settle its debt through the sale of the underlying goods on behalf of the pledgee bank. In fact, the Security Rights Proclamation incidentally mentioned trust receipt under Article 2(27) and recognized it as movable property; however, it is not clear in what context trust receipt is adopted in the proclamation, except that it is characterized as a movable property.

Conclusion

The evidences explored from various sources in this investigation show that the English law and Ethiopian law recognize the document of title function of a bill of lading and the possibility that financing banks in a letter of credit could use it as collateral. Holding a bill of lading as security entitles banks to both contractual and proprietary rights. Contractual rights, including the bank's right to claim delivery of the cargo and bring misdelivery actions, are personal rights available only against the carrier and do not constitute securities in the strict sense.

However, the security interest which the bank establishes on the underlying goods is taken as security in proper and bears a right in rem. Nevertheless, the strength of a bill of lading as a security mechanism for financing banks in a letter of credit transaction is not sufficiently understood and receive due consideration. Unlike other forms of security interests in goods, a financing bank holding a bill of lading as collateral can quickly find itself in an unsecured creditor position under certain circumstances. This article, through a comparative analysis of these circumstances under English law and Ethiopian law, draws insights that inform both legislative moves and practices in maritime commerce.

First, the so-called contractual securities of claiming delivery and bringing misdelivery actions are less effective under English law, whereas it is not an issue in Ethiopia. Under English law, exercising these rights forces the bank to join the carriage contract and assume liabilities as if it were a party to the contract. This burden exposes the bank to unforeseen liabilities, compromising its secured creditor status and uniquely positioning a pledgee of a bill of lading in the realm of pledges. In Ethiopia, first, it is not clear if banks have the right to institute a misdelivery action against the carrier. Unless parties provide in their contract a stipulation in favor of third parties, the carrier may raise the relative effect of the contract as a defense under the rules of the general contract. As a result, it is not clear, under Ethiopian law, whether a bank claiming to enforce its contractual rights will become a party to the carriage contract unless the bill of lading clause itself contains a merchant clause.

Second, if the underlying goods are delivered before the seller transfers the bill of lading to the bank, the bill becomes spent and is merely an empty shell. In this context, the bill, while still existing as a document, does not confer any rights regarding the goods it originally represents. Under English law, COGSA 1992 stipulates that the mere discharge of the cargo does not render the bill of lading spent. Therefore, the bill of lading retains its function as a document of title until the goods are delivered to those lawfully entitled to them. In this regard, Ethiopian law has no specific stipulation.

However, it is possible to discern the fate of a spent bill of lading from the close reading of the Commercial Code provisions and the Maritime Code. The Maritime Code limited its temporal application from the moment of shipment to discharge, leaving issues after discharging unaddressed. Furthermore, discharge of an underlying obligation is a general defense under Article 717 of the Commercial Code for a person, a carrier in a bill of lading, sued under a negotiable instrument. Hence, the position of the Ethiopian law seems unfavorable to financing banks as, once the goods specified on the bill of lading are discharged, makes it stops functioning as a document of title.

Thirdly, title to the goods might have already been transferred to the buyer before the bill of lading was transferred to the bank. If the title is transferred to the buyer before the seller transfers the bill of lading to the bank, the bank cannot establish a security interest in the bill of lading, even if it possesses the bill, as the transferor cannot encumber something to which they no longer have an interest. The position of the English law is that for a bank to have a valid pledge, the transferor, the seller in this context, needs to have a title. Thus, if the seller has no title by the time of the transfer of the bill of lading to the bank, banks will not have a valid pledge right over the bill of lading. When it comes to Ethiopia, the Security Rights Proclamation provides that for anyone granting its asset by way of collateral, it needs to have title, specifically ownership, on it. As a result, it appears that the two legal systems regulate the system almost identically.

Fourthly, the intention of the parties in the sale contract to transfer title to the goods also impacts the security of banks in a letter of credit transaction. Even if the seller transfers possession of the bill of lading to the bank, the bank cannot establish a security interest in the underlying goods if the seller does not intend to transfer title with the bill of lading. Under English law, it is the intention of the parties to the sale contract that determines the transfer of title to the underlying goods. The Ethiopian law is not clear if the intention to transfer matters for the valid creation of security rights.

Finally, the use of trust receipts as security by banks in return for the release of the pledged bill of lading also presents a challenge for financing banks. The English law recognizes the use of trust receipts by financing banks. The issue under English law is that if the buyer fraudulently disposes of the encumbered bill of lading to third parties, under the 1889 Factors Act, the third-party transferee will be better protected than the bank that willingly released possession of the collateral, provided the requirements of good faith and factual or legal power of authority are fulfilled. In Ethiopia, the Security Rights Proclamation mentions a trust receipt as movable property, but it does not specify the context in which it can be used. However, targeting its legal effect, the proclamation provides that if an encumbered bill is transferred to third in good faith, the law gives priority to third parties over the first pledgee. Thus, if banks release possession of the bill of lading for any reason, the law in Ethiopia favors third parties in good faith over pledgee banks, like it is in English law.