

International Trade Documents and eBusiness

Vincent O'Brien

Mr O'Brien is a leading world expert in the Finance of International Trade and Documentary Credits. Within the International Chamber of Commerce in Paris he is held as a top training expert in this complex subject matter.

He is the examiner of The Finance of International Trade and International Trade Practice modules for the Institute of International Trade of Ireland. He is the lead content writer for DCPro, the Multimedia and Internet Based eLearning & reference programme in Documentary Credits of the International Chamber of Commerce Paris. Mr. O'Brien is registered with the centre of expertise for the ICC and is an approved consultant of the Institute of Export in the United Kingdom.

Mr. O'Brien has also carried out a considerable amount of training and consulting assignments for the World Bank (IBRD), EBRD, EU, International Chamber of Commerce, US AID and a number of the major international development banks.

During May 2000, Mr O'Brien was nominated to join the expert working group on the eUCP Project of the International Chamber of Commerce dealing with the presentation of electronic documents under Documentary Credits. This expert working group comprises the leading experts in Documentary Credits from around the globe developing rules for 'B2B' international trade settlements.

Mr O'Brien is part of the advisory board to @Global Trade one of the leading innovators in the development of secure trade payment management systems.

International Trade Documents and eBusiness

....a stumbling block, a challenge or an opportunity?

By Vincent O'Brien

(published in DC Insight the technical journal of the ICC on International Trade Settlements and Documentary Credits)

Serious exporters, large and small offering product to international markets have developed sophisticated straight through export processing systems. Everything from order receipt, credit control, inventory management, freight planning (including carrier's instructions), right up to the printing of sets of paper export documents or the transmission of export related data records can be automated.

This is not a new development!

EDI (Electronic Data Interchange) has for many years facilitated this process and has in turn propelled further significant technological advances.

EDI and subsequent technologies have indeed greased the exporter's wheels for export order processing and fulfilment. Unfortunately, however, exporters continually express frustration when the 'brakes' are applied to the export process because a Documentary Credit is securing the payment for the export transaction. This frustration is compounded because securing payment is invariably, the most important element involved.

I am not blaming bankers, how could I, I am one; but this is the reality. Think about it, has bank document processing and settlement time under Documentary Credits accelerated greatly in the past 20 years? There has been some progress. For instance, the issuing and advising process has gained some efficiency, but no major improvement has been achieved in the time taken to examine, remit and effect the final settlement for documents presented.

As stated, no-one is being blamed - but the reality is that the Documentary Credit process which has always been considered burdensome, has by modern benchmarks become inefficient, costly, and to make matters worse in about 60% of cases the process breaks down in the first instance, that is, on first presentation of documents.

At a banking conference back in 1991 Bernard Wheble, when speaking on technology challenges for trade bankers in respect of transport documents, once again shone with his wisdom and insight when he said *"where the source of the problem is an established commercial practice, possibly pre-dating the first invention of the wheel, the solution demands a change in that practice. Certainly, it should not be a re-invention of the wheel, it should merely be supplying it with new and better tyres"*

The core value proposition of a Documentary Credit, that is, the definite undertaking of a bank provided stipulated documents are presented containing data which evidences certain facts or actions remains fully valid today.

The exporter has obviously greased his export wheels, maybe all the Documentary Credit needs is to be fitted with 'new and better tyres' as Bernard Wheble suggested back in 1991.

The advent of the Internet, on-line markets with all the in-built speed and efficiency in marketing, communications, logistics control will provide the ultimate challenge but also an opportunity to the Documentary Credit. The Documentary Credit can and will rise to this challenge, because it must.

Trading today, either on the Internet or off-line, requires the exporter to anticipate the demand for their product with pin-point accuracy. Stock levels must be constantly monitored to ensure that there is always enough product to ship. The exporter must know the latest shipment date and exactly how long shipment will take. The exporter is demanding the capability to track their product as it moves through the supply chain from place of dispatch to place of final destination. This is easily achieved through web enabled technology.

So, what needs to be done to fit new and better tyres to the Documentary Credit?

First, the rules that apply to the presentation of documents, electronic, paper or both need to be in place. On this front the ICC is moving fast. An ICC working group led by Dan Taylor and Rene Muller has already released with electrifying speed and efficiency the draft "UCP Supplement for Electronic Presentation" or eUCP to ICC national committees for 'electronic' return comments. Comments have been significant and are currently being incorporated.

Second, integrated straight through document checking and processing systems must be implemented, which will seamlessly process export documents or electronic data records issued by all parties in the Documentary Credit chain, examine them for compliance and effect final settlement. This is a technology challenge, not a reinvention of the wheel. It is an evolution from the paper environment, through possibly a mixed paper-electronic environment to an eventual end-to-end electronic documentary credit presentation process.

Third, the essential ingredients for secure international trading and in particular 'on-line' trading are 'Trust' and 'Faith'. The integrity of the Documentary Credit which constitutes a definite bank undertaking of payment must be reinforced at every opportunity. For exporters to agree to the use of a Documentary Credits as a mainstream business to

3 UNCTAD - Expert Meeting on Electronic Commerce and International Transport Services - vob@gtilearning.com
business payment instrument in the electronic world, exporters must trust the party issuing the Credit, but more importantly the exporter who is the ultimate beneficiary, must have faith in the Documentary Credit process itself.

Our faith is moulded by our experiences and learning.

The Documentary Credit as we know it, is today facing its greatest challenge. The Documentary Credit can and will rise to this challenge.

As closing remarks to his conference presentation back in 1991, Bernard Wheble proclaimed *"So perhaps, rather than seeing legal obstacles to technology as a "stumbling block", we bankers may see them as a "challenge" ... and like every self-respecting Irishman, join in the fight"*

I guess, being an Irishman makes joining in the fight, the natural thing to do!

Vincent O'Brien: vob@gtilearning.com

TRUST ME - The use of traditional paper transport documents to secure international trade transactions.

By: Robert M. Parson who is head of the legal team with @Global Trade.

For many years banks have followed the practice of releasing goods to their customers in circumstances where the title documents, be they bills of lading or bearer warehouse warrants, are pledged to the bank as security. However, in order to enable the customer to sell the goods and to present the bill of lading or warrant against payment, the bank has to release these documents. In doing so, the bank seeks to secure its position at least in the case where the customer goes bankrupt before the funds have been received under the sale.

This procedure, under which the bank agrees to release the title documents against the customer entering into a _trust receipt_ has led to confusion in the minds of some bankers and their customers as to precisely what rights remain vested in the bank once the customer has been put in possession of the title documents to sell them. This month we examine the different rights that exist before and after the trust receipt is entered into and consider how the banks can best protect their position when the practicalities of the particular trade require them to release the title documents to the customer.

The Bank's Pledge Security

When a customer pledges goods and title documents to a bank it gives the bank title to the goods as pledgee. In some cases banks may not have a pledge instrument in place, but nevertheless intend to exercise rights as holders of the bills of lading and thereby obtain rights against the goods pending reimbursement - for example, in a letter of credit transaction where they have paid for the documents on the customer's behalf and where customer will ultimately reimburse them through the sale proceeds. If there is no pledge in place at that time, a bank releasing the bill of lading to the customer gives up its entire security. In this case, ensuring that the bank

4 UNCTAD - Expert Meeting on Electronic Commerce and International Transport Services - vob@gtilearning.com
releases the goods under a _trust receipt_ to record the nature of its interest in the documents is essential.

The aim is to ensure that the bank is protected in the event of the customer's bankruptcy because the nature of the relationship between the bank and the customer, be it under a pledge or a trust receipt or both, is such that it will be largely invisible to other parties dealing with the customer and to the liquidator. If the goods and documents are actually pledged to the bank and the bank releases the title documents to the customer to enable it to sell them as the bank's agent, then in the event of a bankruptcy the bank is still protected and the special property rights that the bank obtains through the pledge will enable it to recover the value of the goods. If there is no pledge the bank is not protected.

What the trust receipt does therefore is to provide the bank with rights against the bankruptcy of the buyer when those special property rights would not otherwise exist (e.g. under a pledge). In essence it is an agreement that will bind the customer's administrator or liquidator and that recognises that the bank retains its possessory title over the documents despite having released them into the hands of the customer.

No Protection against Fraud of the Customer

Where the bank will not be protected, however, is where the customer, instead of selling the goods and holding the funds to the bank's order parts company with the goods and the documents and diverts the funds away from the bank. In that event, the bank will have no rights against the new holder of the documents or goods whether this holder obtained them by purchase or pledge without notice of the bank's interest.

At first sight this seems to run counter to the terms of English law which provide that a sale by a person who is not the owner of the goods cannot pass good title to the buyer unless the actual owner of the goods consents to the sale. However, Section 21 of the Sale of Goods Act 1979 makes clear that the owner of the goods (and for these purposes read bank for owner) can be precluded by his conduct from denying the authority of his customer to sell the goods. First, where the seller of goods is left in possession of the goods and the title documents after the sale or pledge has been completed, any third party taking the goods in turn by sale or pledge without notice of the previous sale or pledge is entitled to assume that the real owner or pledgee of the goods has authorized the sale (Section 24 Sale of Goods Act 1979).

A far older piece of legislation, the Factors Act 1889 (Section 2 (1)), provides that where the sale or pledge or disposition of the goods is made in the ordinary course of business by the party left in possession of the goods then the party taking the goods on sale or pledge can do so as if the party giving him the goods or documents was expressly authorized by the owner.

To see an example of how that works between two banks it is worth looking at the case of Lloyd's Bank -v- Bank of America National Trust and Savings Association [1938] 2KB 147 where Lloyd's Bank released shipping documents to its customer, Strauss & Co Ltd, in exchange for a trust receipt. The idea of releasing the goods was to enable Strauss & Co to resell the goods, but instead of doing that they fraudulently pledged the shipping documents to another bank, Bank of America National Trust & Savings Association, and were

thereby able to raise further money on the goods - a double pledge. Strauss & Co Limited then went into liquidation and Lloyd's Bank sued the Bank of America for return of the shipping documents. However, the English Court of Appeal held that ownership of the documents and the goods represented by them had passed to the Bank of America.

In that case it was perfectly clear from the terms of the trust receipt that Lloyd's Bank had released the bills of lading to Strauss & Co _in order to enable the company to sell the merchandise as trustees for the Plaintiffs [0]_ . For those familiar with English trust law this produced for Lloyd's Bank an _equitable title_ to the goods. Nonetheless this did them no good in the face of the Bank of America's taking up of the documents in good faith because the Bank of America was entirely unaware of Lloyd's Bank's interest.

It followed that the Bank of America obtained legal title to the goods pursuant to Section 2 (1) of the Factors Act 1889 so the trust receipt afforded Lloyd's Bank no protection against their customer's fraud.

Retention of Title

The position is essentially no different than under any retention of title provision of the type which have become common place in international sale of goods. Even if the terms of the trust receipt require payment of funds to be into a specific account upon the sale, the bank is essentially only protected so long as the purchaser of the goods from the customer is aware of the nature of the trust and the requirement to pay the proceeds through the bank's account. The bank, once the goods have been sold loses both its legal and equitable property in the goods but obtains an equitable right over the proceeds of sale under the trust receipt. If the customer so conducts himself as to avoid the mechanism through which the bank would normally see the payment then the bank is going to be left out of pocket.

This issue tends to arise more frequently in cases where trading companies are using a large number of different banks to finance their operations. As a result banks need to consider very carefully the arrangements that they have in place. The only real safeguard is to ensure that the documents are not in fact released against a trust receipt but are released pursuant to an undertaking given to the buyer that will only be acted upon once funds are actually received in the customer's bank account with the bank.

Transport Documents , Transport Records and Transport Data will develop hand in hand with customs and practice of the international trading community. Rules, regulations and law can facilitate this process but it is faith and trust that will ultimately drive developments.

Vincent O'Brien 17-09-2001