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Navigating Potential Risks When Lending Against Goods on the Water Covered by Sea Waybills, Rather Than Bills of Lading – Part I

By Peter J. Lahny, IV

In this two-part article,¹ the author addresses how secured creditors might try to mitigate the risks associated with lending against goods in transit located in international waters covered by a sea waybill rather than by a bill of lading. In this first part, the author briefly addresses the differences between bills of lading and sea waybills and then discusses in detail the issues created for secured creditors in lending against such goods covered by sea waybills. In the conclusion, the author will make specific suggestions to try to mitigate certain risks created by the use of sea waybills.

In historical asset-based lending transactions, secured creditors have typically only been willing to lend against goods in transit located in international waters to the extent that such goods were covered by:

- (i) negotiable documents of title² (e.g. bills of lading,³ etc.) that have been issued or endorsed to the order of the secured creditor;
- (ii) non-negotiable bills of lading issued in the name of the secured creditor;⁴ or

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¹ This two-part article will conclude in the next issue of The Banking Law Journal.

² Section 1-201(16) of the Uniform Commercial Code, as adopted in the State of New York (U.C.C.) defines “document of title” to include:

[B]ill of lading, dock warrant, dock receipt, warehouse receipt or order for the delivery of goods, and also any other document which in the regular course of business or financing is treated as adequately evidencing that the person in possession of it is entitled to receive, hold, and dispose of the document and the goods it covers. To be a document of title, a document must purport to be issued by or addressed to a bailee and purport to cover goods in the bailee’s possession which are either identified or are fungible portions of an identified mass.

³ Section 1-201(6) of the U.C.C. defines “bill of lading” as “a document evidencing the receipt of goods for shipment issued by a person engaged in the business of transporting or forwarding goods.” Section 9-102(3) of the U.C.C. defines “document” to mean “a document of title or a receipt of the type described in Section 7-201(2).”

⁴ Section 7-104 of the U.C.C. reads as follows:

§ 7-104. Negotiable and Nonnegotiable Document of Title.

- (a) A document of title is negotiable if by its terms the goods are to be delivered to bearer or to the order of a named person.
- (b) A document of title other than one described in subsection (a) is nonnegotiable. A bill

- (iii) a trust receipt⁵ delivered to the creditor with respect to the original bills of lading, pursuant to a master trust receipt agreement,⁶ in form and substance satisfactory to the secured creditor.

This was, and continues to be, the market standard since, (a) negotiable bills of lading are documents of title, granting the holder of original bills of lading legal title to the underlying goods;⁷ and (b) bills of lading are by far the most common (and important) documents used in international shipping.

However, as the speed and technology of the shipping industry has improved and the world of international trade has condensed,⁸ the use of sea waybills,⁹

of lading that states that the goods are consigned to a named person is not made negotiable by a provision that the goods are to be delivered only against an order in a record signed by the same or another named person.

- (c) A document of title is nonnegotiable if, at the time it is issued, the document has a conspicuous legend, however expressed, that it is nonnegotiable.

U.C.C. § 7-104.

⁵ See Henry Gabriel, Article: The Development of the American “Security Interest” and its Effect on the International Harmonization of Security Rights 17 *Brook. J. Corp. Fin. & Com. L.* 39, 41 (October 2025) (stating that the “trust” was a two-step process where the bank legally held the bill of lading, and title to the goods while the buyer had actual possession of the bill of lading, allowing the buyer to get possession of the goods and resell them.”).

⁶ See Peter J. Lahny, IV, Navigating Intercreditor Arrangements in Commodities & Trade Finance: A Practical Guide, 142 *The Banking L. J.* 384, 389 n. 21 (October 2025) (stating that “a master trust receipt agreement is a very specific type of security agreement that acknowledges that a secured party has been furnished with original documents of title to perfect its security interest in certain underlying goods, and provides for the return of the documents of title to the debtor under specific circumstances. The provisions of the master trust receipt agreement will grant the secured party a security interest in the underlying goods during the period that the documents of title are being used by the debtor for the specific purposes set forth therein.”).

⁷ See *supra* note 2.

⁸ See Stasia M. Williams, Something Old, Something New: The Bill of Lading in the Days of EDI 1 *Transnat’l L. & Contemp. Probs.* 555, 564-65 (Fall 1991) (discussing technological changes in the shipping industry).

⁹ See Vasileios Ziakas, Security Alternatives of Sea Waybill and Straight Bill of Lading, 4 *Journal of International Trade, Logistics and Law* 13, 13 (2018) (providing a comprehensive definition of sea waybill as follows: “The sea waybill is a non-negotiable transport document and its great advantage is that its presentation by the consignee is not required in order for him, on production of satisfactory identification, to take delivery of the goods, thus avoiding delay both for him and the carrier where the goods arrive before the waybill. It is not a document of title but contains, or is evidence of, the contract of carriage as between the shipper and carrier in that it incorporates the standard terms of the carrier on its face. However, unlike a bill of lading, these terms are not detailed on the reverse of the waybill which is blank. A waybill is usually issued in

rather than bills of lading, has become much more common.¹⁰ The use of sea waybills can eliminate certain shipping delays (and the costs associated therewith) that are often created due to the requirement for presentation of original documents that is necessitated by the use of bills of lading.¹¹ This has forced many secured creditors, specifically in the commodities and trade finance arenas, to try to adjust to the additional risks that must be overcome when lending against goods in transit located in international waters, and which are not covered by a document of title. Unfortunately, many times, the secured creditor's response is to simply revise the definition of "Eligible Inventory" set forth in its loan documentation to add a reference to "sea waybills" in the subsection setting forth the requirements for the borrower's in transit inventory to be Eligible Inventory. This accommodation ignores all of the additional risks associated with lending against goods located in international waters that are covered by sea waybills rather than bills of lading.

This two-part article addresses how secured creditors might try to mitigate the risks associated with lending against such goods covered by a sea waybill. In this first part, the article briefly addresses the differences between bills of lading and sea waybills and then discusses in detail the issues created for secured creditors in lending against such goods covered by sea waybills. The conclusion of this article will make specific suggestions to try to mitigate certain risks created by the use of sea waybills.

I. BILLS OF LADING VERSUS SEA WAYBILLS – A BRIEF OVERVIEW

Typically, secured creditors are only willing to lend against assets over which the applicable secured creditor maintains a first priority, perfected security interest.¹² Accordingly, when lending against goods in transit located in international waters, a secured creditor's first impulse will always be to require

the 'received for shipment' form but may, like a bill of lading, be notated once the goods have been loaded").

¹⁰ See generally Ziakas, *supra* note 9.

¹¹ See generally Williams, *supra* note 8, at 565.

¹² Section 9-312(c) of the U.C.C. reads as follows:

(c) Goods covered by negotiable document. While goods are in the possession of a bailee that has issued a negotiable document covering the goods:

(1) a security interest in the goods may be perfected by perfecting a security interest in the document; and

(2) a security interest perfected in the document has priority over any security interest that becomes perfected in the goods by another method during that time.

U.C.C. § 9-312(c).

that such goods be covered by negotiable bills of lading that have been issued or endorsed to the order of the secured creditor, thereby granting the secured creditor legal title to the underlying goods.¹³ While there are certain exceptions, this remains the market standard.¹⁴ However, with the emergence of the use of sea waybills in international shipping, secured creditors in the commodities and trade finance space have been forced to re-think how to mitigate the risks created by lending against goods on the water that are not covered by bills of lading. This section will briefly discuss the differences among negotiable bills of lading, non-negotiable bills of lading, trust receipts and sea waybills.

A. Negotiable Bills of Lading

Pursuant to Section 7-104(a) of the U.C.C., “[a] document of title is negotiable if by its terms the goods are to be delivered to bearer or to the order of a named person.”¹⁵ In the typical asset-based lending transaction, most secured creditors prefer goods on the water to be covered by negotiable bills of lading. As discussed above, from the secured creditor’s point of view, the most important aspect of a negotiable bill of lading is that it is a document of title.¹⁶ That fact alone has, for many years, given secured creditors all the comfort that they need to confidently lend against goods in transit in international waters.

In an ideal world, the secured creditor would require that (a) the negotiable bill of lading be issued or endorsed to the order of the secured creditor, and (b) the secured creditor take possession of the full set of original 3/3 bills of lading in respect of any shipment that such secured creditor is financing.¹⁷ Taking possession of the original bills of lading ensures that no other creditor will have

¹³ See generally Williams, *supra* note 8, at 561–62.

¹⁴ See Romina Mohan Gopalan, *The Bill of Lading’s Role in Securing Trade Finance: A Business Guide*, Drip Capital Blog (May 28, 2025), <https://www.dripcapital.com/en-us/resources/blog/bill-of-lading>.

¹⁵ U.C.C. § 7-104(a).

¹⁶ See *supra* note 2; see also Williams, *supra* note 8, at 561–62 (stating that “[a]s a document of title: (a) it represents the goods, allowing the buyer to deal with the goods while they are at sea; (b) it transfers constructive possession of the goods; (c) it may operate to transfer property in the goods if it is the intention of the parties to do so.”).

¹⁷ Section 9-313(a) of the U.C.C. reads as follows:

(a) Perfection by possession or delivery. Except as otherwise provided in subsection (b), a secured party may perfect a security interest in negotiable documents, goods, instruments, money, or tangible chattel paper by taking possession of the collateral. A secured party may perfect a security interest in certificated securities by taking delivery of the certificated securities under Section 8-301.

U.C.C. § 9-313(a).

a superior security interest in the underlying goods.¹⁸ However, given the speed at which goods now reach the applicable ports of destination and the fact that original bills of lading must be produced at the time of delivery of the underlying goods, in my experience, many times secured creditors will permit the borrower to have the negotiable bills of lading issued to the “order” of the borrower and to maintain possession of the original bills of lading pursuant to a trust receipt. The use of the trust receipt will be discussed in Section I.C. below.

The negotiable bill of lading itself also (i) acts as a binding contract of carriage between the shipper and the carrier, and (ii) acts as a receipt for the underlying goods that confirms that the goods have been received in good condition.¹⁹ In its capacity as a contract of carriage, the bill of lading evidences the terms of the shipment of the underlying goods.²⁰ In its capacity as a receipt for the underlying goods, the bill of lading “provides details about quantity, identifying marks, volume, weight, description, and apparent condition of the cargo.”²¹ To the extent that there is any visible damage to the cargo, the carrier must note such damage on the face of the bill of lading prior to acceptance.²² If no damage is listed, the carrier cannot claim prior damage when the goods arrive at their final destination.²³ Apart from those notations and any required endorsements, any material changes to the terms of a negotiable bill of lading will require the return and re-issuance of the full set of originals.²⁴

A negotiable bill of lading must identify each of the shipper / supplier, the carrier, and the receiver / consignee, to whose “order” the negotiable bill of lading will be made.²⁵ Since a negotiable document of title entitles the person in possession of it to receive, hold, and dispose of the document and the underlying goods that it covers, the underlying goods can be sold and re-sold

¹⁸ Section 9-312(c)(2) of the U.C.C. reads as follows: “(2) a security interest perfected in the document has priority over any security interest that becomes perfected in the goods by another method during that time.” U.C.C. § 9-312(c)(2).

¹⁹ See Williams, *supra* note 8, at 561 (stating that “[i]n addition to its use as a receipt and a contract of carriage, the bill of lading serves the unique function of a document of title.”).

²⁰ See Williams, *supra* note 8, at 561.

²¹ See Williams, *supra* note 8, at 560.

²² See Williams, *supra* note 8, at 561.

²³ See Williams, *supra* note 8, at 561.

²⁴ Peregrine Storrs-Fox, When can you change the details in a bill of lading?, TT Talk (Jan. 20, 2004), <https://www.ttclub.com/news-and-resources/news/article/tt-talk-when-can-you-change-the-details-in-a-bill-of-lading/>.

²⁵ See Williams, *supra* note 8, at 560.

while still in transit.²⁶ Specifically, in the commodities finance context, the negotiability aspect is key. This is due to the fact that, in many cases, shipments of commodities will be sold and ownership of the goods will transfer while the goods are on route to the applicable final destination.²⁷

B. Non-Negotiable Bills of Lading

Pursuant to Section 7-104(b) and (c) of the U.C.C., a document of title is non-negotiable if (i) by its terms, the goods are *not expressly* to be delivered to bearer or to the order of a named person, or (ii) at the time the bill of lading is issued, the bill of lading has a conspicuous legend, however expressed, that it is non-negotiable.²⁸ Non-negotiable bills of lading are often referred to as “straight” bills of lading, while negotiable bills of lading are often referred to as “order” bills of lading.²⁹

By definition, ownership of a “non-negotiable” bill of lading and the underlying goods that it covers cannot be transferred during the shipment of the goods.³⁰ Only the person originally named as consignee on the face of the non-negotiable bill of lading can present the original bills of lading and claim the underlying goods at the final port of destination.³¹ Due to the fact that the non-negotiable bill of lading lacks the negotiability aspect of the negotiable bill of lading, it is not as useful in the commodities finance context. The non-negotiable bill of lading is most useful in intercompany/affiliate transactions or in container shipping transactions where transfer of ownership during transport is much less likely.³²

Since non-negotiable bills of lading are also documents of title, secured creditors have been able to get comfortable lending against the underlying goods in certain circumstances. When lending against the goods covered by a non-negotiable bill of lading, the secured creditor will require that the non-negotiable bills of lading be issued either in the name of the secured creditor or the borrower.³³ When the non-negotiable bill of lading is issued in the name of the borrower, it is again typical for the secured creditor to allow the

²⁶ See *supra* note 2; see also Williams, *supra* note 8, at 561-62.

²⁷ See Williams, *supra* note 8, at 562 and 566.

²⁸ U.C.C. § 7-104.

²⁹ See Ziakas, *supra* note 9 at 16.

³⁰ See Williams, *supra* note 8, at 562.

³¹ See Ziakas, *supra* note 9 at 16.

³² See Williams, *supra* note 8, at 566.

³³ See Commercial Law League of America, Gen. Editors, Commercial Law and Practice Guide Ch. 25 § 25.03 (Matthew Bender) (2026); see also Boris Kozolchyk, Supply Chain

borrower to maintain possession of the original bills of lading pursuant to a trust receipt (as discussed in Section I.C. below).

C. Trust Receipts

The Merriam-Webster.com Legal Dictionary, defines a “trust receipt” as “a trust agreement between a lender and a borrower by which the lender gives up possession of goods without abandoning title and the borrower agrees to hold the goods in trust for the lender and if the goods are sold to turn the proceeds over to the lender in settlement of the debt.”³⁴ Due to the speed at which goods now reach their final ports of destination and the fact that original bills of lading must be produced at the time of delivery of the underlying goods, many times secured creditors will permit the borrower to take possession of the original bills of lading pursuant to a trust receipt.³⁵ The secured creditor will only permit this arrangement to the extent that the borrower has entered into a master trust receipt agreement with the secured creditor, and only for the specific purposes set forth therein. Those purposes will typically include the following:

- (i) to allow for transfer of the goods to an independent third-party carrier for transportation;
- (ii) to arrange for inspection of the goods by appropriate customs officials from governmental agencies;
- (iii) to arrange for the storage of the goods represented by the documents of title in a public warehouse;
- (iv) to arrange for the sale of the goods represented by the documents of title in the borrower’s ordinary course of business; or
- (v) for such other purpose(s) as to which the secured creditor shall from time to time agree in writing, in its sole discretion.

Pursuant to the terms of the master trust receipt agreement, in exchange for the original bills of lading, the borrower will provide the secured creditor with a “trust receipt.”³⁶ The trust receipt must be substantially in the form attached to the applicable master trust receipt agreement. It is essential that the trust

Financing, Straight Bills of Lading and Standby Letters of Credit, 2 Geo. Mason J. Int’l Com. L. 100, 108 (Spring 2011).

³⁴ See Trust Receipt, Merriam-Webster.com Legal Dictionary (<https://www.merriam-webster.com/legal/trust%20receipt>) (last visited July 26, 2026).

³⁵ See Jacob Rabkin, et. al., 1 Rabkin & Johnson, Current Legal Forms with Tax Analysis § 5C.06 (Matthew Bender) (2026).

³⁶ Id.

receipt be completely and correctly filled out by the borrower and also duly executed by an authorized officer of the borrower / trustee. The trust receipt will contain a detailed description of the applicable bill of lading and the underlying goods, and will contain an express grant of a continuing security interest to the secured creditor in both the bill of lading and all of the underlying goods.

The purpose of the trust receipt is to allow the borrower / trustee to actually possess the bill of lading, thereby allowing the borrower to obtain possession of the goods while contractually agreeing that the secured creditor continues to have rights under the bill of lading and title to the underlying goods.³⁷ To ensure that the secured creditor continues to be perfected in the underlying goods, the secured creditor will (i) make the documents of title available to borrower solely for the express purpose of “ultimate sale or exchange” or the “loading, unloading, storing, shipping, transshipping, manufacturing, processing, or otherwise dealing” with the goods “in a manner preliminary to their sale or exchange”; and (ii) require that the goods are actually received by the borrower within the 20-day temporary perfection period granted under Section 9-312(f) of the U.C.C.³⁸

In an attempt to avoid the shipping delays and associated costs referred to above, the use of trust receipts has become very common in typical lending transactions. Again, the speed at which goods reach the final ports of

³⁷ See Gabriel, *supra* note 5, at 41; see also Gabriel, *supra* note 5, at 41 n.9 (stating that “I have always thought the trust receipt is the most ingenious of security devices. If the bank has possession of the bill of lading as a pledgee, the buyer cannot get possession of the goods to resell them. If the bank gives the possession of the bill of lading to the buyer, the bank no longer has possession and loses the security rights of a pledgee. The solution is to create a trust receipt by which the buyer only holds the documents in trust for the bank and only for the limited purpose of getting the goods to resell them. In the case of a trust receipt, the effect of possession provides some of the benefits of possession without others. The legal effect of possession depends on the purpose for which you ask the question. The trust receipt beautifully captures the essence of the common law trust, the wonderful division of legal and beneficial rights. It, of course, lays waste to the general rules of possession that govern documents of title.”).

³⁸ Section 9-312(f) of the U.C.C. reads as follows:

(f) Temporary perfection: goods or documents made available to debtor. A perfected security interest in a negotiable document or goods in possession of a bailee, other than one that has issued a negotiable document for the goods, remains perfected for 20 days without filing if the secured party makes available to the debtor the goods or documents representing the goods for the purpose of:

- (1) ultimate sale or exchange; or
- (2) loading, unloading, storing, shipping, transshipping, manufacturing, processing, or otherwise dealing with them in a manner preliminary to their sale or exchange.

U.C.C. § 9-312(f).

destination has made it impractical in many cases for the secured creditor to obtain and then re-deliver the original bills of lading in time for such goods to be promptly offloaded.

D. Sea Waybills

Vasileios Ziakas provided a simple definition of “sea waybill” as follows: “[a] non-negotiable document which evidences a contract for the carriage of goods by sea and the taking over or landing of the goods by the carrier, and by which the carrier undertakes to deliver the goods to the consignee named in the document.”³⁹ Article 21 of the Uniform Customs and Practice for Documentary Credits effective July 1, 2007 (UCP 600) also defines “Non-Negotiable Sea Waybills” and provides a further description of certain provisions that must be included in a non-negotiable sea waybill.⁴⁰ The most important distinction

³⁹ See Ziakas, *supra* note 9 at 13.

⁴⁰ Article 21 of the Uniform Customs and Practice for Documentary Credits effective July 1, 2007 (UCP 600) defines a “Non-Negotiable Sea Waybill” as follows:

a. A non-negotiable sea waybill, however named, must appear to:

i. indicate the name of the carrier and be signed by:

- the carrier or a named agent for or on behalf of the carrier, or
- the master or a named agent for or on behalf of the master.

Any signature by the carrier, master or agent must be identified as that of the carrier, master or agent.

Any signature by an agent must indicate whether the agent has signed for or on behalf of the carrier or for or on behalf of the master.

ii. indicate that the goods have been shipped on board a named vessel at the port of loading stated in the credit by:

- pre-printed wording, or
- an on board notation indicating the date on which the goods have been shipped on board.

The date of issuance of the non-negotiable sea waybill will be deemed to be the date of shipment unless the non-negotiable sea waybill contains an on board notation indicating the date of shipment, in which case the date stated in the on board notation will be deemed to be the date of shipment. If the non-negotiable sea waybill contains the indication “intended vessel” or similar qualification in relation to the name of the vessel, an on board notation indicating the date of shipment and the name of the actual vessel is required.

iii. indicate shipment from the port of loading to the port of discharge stated in the credit.

If the non-negotiable sea waybill does not indicate the port of loading stated in the credit as the port of loading, or if it contains the indication “intended” or similar qualification in relation to the port of loading, an on board notation indicating the port of loading as stated in the credit, the date of shipment and the name of the vessel is required. This provision applies even when loading on board or shipment on a named vessel is indicated by

between a sea waybill and a bill of lading is that, while a sea waybill also acts as a receipt for the underlying goods and a binding contract of carriage between the shipper and the carrier, a sea waybill is *not* a document of title.⁴¹

In most respects, including general appearance, a sea waybill is very similar to a non-negotiable bill of lading.⁴² However, since a sea waybill is not a document of title, certain terms of the sea waybill can be modified by the shipper and the carrier while the goods are on route, without needing to reissue a new original document of title.⁴³

It is also important to note that, since a sea waybill is not a document of title, it does not convey any ownership rights with respect to the underlying goods to the holder of the original sea waybill.⁴⁴ As such, to receive the underlying goods, the consignee does not need to produce any originals.⁴⁵ The consignee is merely required to prove that he/she is the party named in the sea waybill.⁴⁶

pre-printed wording on the non-negotiable sea waybill.

iv. be the sole original non-negotiable sea waybill or, if issued in more than one original, be the full set as indicated on the non-negotiable sea waybill.

v. contain terms and conditions of carriage or make reference to another source containing the terms and conditions of carriage (short form or blank back non-negotiable sea waybill). Contents of terms and conditions of carriage will not be examined.

vi. contain no indication that it is subject to a charter party.

b. For the purpose of this article, transshipment means unloading from one vessel and reloading to another vessel during the carriage from the port of loading to the port of discharge stated in the credit.

c.

i. A non-negotiable sea waybill may indicate that the goods will or may be transhipped provided that the entire carriage is covered by one and the same non-negotiable sea waybill.

ii. A non-negotiable sea waybill indicating that transshipment will or may take place is acceptable, even if the credit prohibits transshipment, if the goods have been shipped in a container, trailer or LASH barge as evidenced by the non-negotiable sea waybill.

d. Clauses in a non-negotiable sea waybill stating that the carrier reserves the right to tranship will be disregarded

UCP 600 Article 21.

⁴¹ See Williams, *supra* note 8, at 566.

⁴² See generally Ziakas, *supra* note 9.

⁴³ See Ziakas, *supra* note 9 at 15.

⁴⁴ See Ziakas, *supra* note 9 at 14.

⁴⁵ See Williams, *supra* note 8, at 566.

⁴⁶ See Williams, *supra* note 8, at 566; see also Ziakas, *supra* note 9 at 14.

Also, sea waybills are non-negotiable, so in nearly all cases, only the named consignee can retrieve the goods.⁴⁷

Since originals do not need to be produced at the time of delivery, the use of sea waybills can significantly reduce delays during the offloading process. Accordingly, the use of sea waybills effectively eliminates the potential shipping delays and additional costs typically associated with bills of lading.⁴⁸ This has been a major reason for the rise in the use of sea waybills in international shipping across nearly all industries.⁴⁹

II. RISKS ASSOCIATED WITH LENDING AGAINST GOODS COVERED BY SEA WAYBILLS

Typically, secured creditors are unwilling to lend against goods covered by sea waybills, due to the increased risks created by lending against in transit goods that are not covered by a document of title.⁵⁰ This is obviously the correct position for the secured creditor to take. However, with the increase in the frequency of use of the sea waybill in international shipping, particularly in the commodities and trade spaces, secured creditors are being forced to try to get more comfortable with lending against those underlying goods. This Section II. identifies certain risks presented by the use of the sea waybill, rather than the bill of lading. Section III., to be published in the conclusion of this article, will focus on steps that the secured creditor can take to try to mitigate the risks laid out in this Section II.

A. Lack of a Perfected, First Priority Security Interest in Underlying Goods

As discussed above, the most difficult hurdle for the secured creditor to overcome in lending against goods in international waters that are covered by sea waybills is the fact that sea waybills are not documents of title.⁵¹ Due to the fact that sea waybills are not documents of title, they do not transfer title to underlying goods to the holder of the sea waybill.⁵² Accordingly, the secured creditor will *not* have a first priority, perfected security interest in the underlying

⁴⁷ See Ziakas, *supra* note 9 at 14.

⁴⁸ See Williams, *supra* note 8, at 566.

⁴⁹ See William P. Streng et al., 1 *International Business Planning: Law and Taxation* § 5.13 (Matthew Bender, Rev. Ed.).

⁵⁰ *Id.*

⁵¹ See Ziakas, *supra* note 9 at 14.

⁵² See Ziakas, *supra* note 9 at 14.

goods while they are in transit in international waters.⁵³ In a syndicated loan facility, this can create major issues for the lender group.

In nearly all cases, each of the lenders in the syndicate will have obtained internal credit approvals for the making of advances against collateral over which the Agent maintains a first priority, perfected security interest. Accordingly, this arrangement would typically require the various lenders to obtain additional approvals to lend against unperfected, in transit inventory. Since this category of eligible inventory would typically only account for a very small fraction of the borrowing base in a syndicated facility, it can be easily overlooked in the review process by the lenders and their counsel.

To the extent that the secured creditor / Agent does not have a first priority, perfected security interest in the underlying goods, it would potentially be lending into a second lien position or worse. It is also important to note that, while the goods are located in international waters (and not covered by a bill of lading), any security interest that the secured creditor / Agent may possess in such goods will be unperfected. For any secured creditor, providing funding against collateral in which such secured creditor's security interest is not in the first lien position, or worse is unperfected, is a cardinal sin of secured lending.

When analyzing the risk set forth in this Section II.A. above, a secured creditor must take into consideration the fact that this is a timing issue, since the secured creditor's security interest in the underlying goods will be perfected upon the goods being delivered to the borrower in a port in the U.S. or another jurisdiction where the secured creditor has properly perfected its security interest in such goods. However, the borrower will typically want the secured creditor to finance the purchase of the goods prior to shipment. For the secured creditor, getting comfortable providing the requested advances requires accepting the fact that, for the period of time the goods are in international waters, the secured creditor will not have a properly perfected security interest in the collateral securing its loan.

It is also important to note that there are other circumstances where a secured creditor may be willing to lend against goods on the water over which it does not maintain a perfected security interest. These include a secured creditor lending against goods covered by bills of lading, issued in the name of the borrower, but only requiring that the borrower provide the secured creditor with copies of such bills of lading. In those circumstances, similar to when a secured creditor is lending against goods covered by a sea waybill, the secured creditor is agreeing to be unsecured against the underlying goods while they are

⁵³ See generally Section 9-312 of the U.C.C., *supra* note 12.

on the water. However, this only occurs when the relationship between the secured creditor and the borrower is very strong, and due to that relationship, the secured creditor is willing to accept the additional risk for the limited period while the goods are actually on the water. By agreeing to lend against copies of bills of lading, the secured creditor is actually agreeing to lend into a worse position than is being proposed by this article in respect of lending against sea waybills. As such, this provides a good example of the typical secured creditor's willingness to get creative when lending against goods on the water.

However, the fact that none of this is an issue when the applicable goods are covered by a negotiable bill of lading clearly adds a layer of complexity to the applicable secured creditor's analysis.

B. Diversion of the Underlying Goods by the Shipper

Another major hurdle for the secured creditor to overcome is the ease with which the shipper / supplier can divert the applicable goods to a different port of destination.⁵⁴ When goods are covered by a sea waybill, "the shipper is entitled to request redelivery of the goods until the time of their arrival at the place of delivery designated ad hoc in the contract."⁵⁵ Since it is not a document of title, certain terms of the sea waybill can be changed by the shipper and the carrier while the goods are on route, without needing to return and reissue an original document of title, as would be required when using a bill of lading.⁵⁶

Obviously, it is very difficult for a secured creditor to get comfortable with lending against goods that can be diverted by a third party to a foreign jurisdiction without their knowledge or approval. While there are many reasons why the shipper / supplier might legitimately need to divert the underlying goods, none of them are good for the secured creditor that financed those goods assuming they will reach their stated destination. The uncertainty that this creates just adds to the secured creditor's reservations about lending against goods covered by sea waybills in the first place. Also, while this could be viewed as typical fraud risk, this risk is much less likely when dealing with bills of lading since, as mentioned above, such changes typically require the return and re-issuance of the full set of originals.⁵⁷

⁵⁴ See Ziakas, *supra* note 9 at 15.

⁵⁵ See Ziakas, *supra* note 9 at 15.

⁵⁶ See Ziakas, *supra* note 9 at 15.

⁵⁷ See Storrs-Fox, *supra* note 24.

C. Issues Created by the Standard Form of Transactional Commodities Finance Intercreditor Agreement

Very specific issues are created by the use of sea waybills rather than bills of lading in the context of commodities and trade finance. Under the standard form of transactional commodities finance intercreditor agreement, the most senior Specific Security Interest⁵⁸ in the underlying goods is granted to the secured creditor in possession of a tangible negotiable document of title, or the secured creditor in whose name a non-negotiable document of title has been issued.⁵⁹ Accordingly, when shipping goods subject to a bill of lading, taking possession of the original negotiable bill of lading will ensure that the applicable secured creditor maintains the most senior Specific Security Interest under the standard form of transactional commodities finance intercreditor agreement.⁶⁰

Another article I wrote, “Navigating Intercreditor Arrangements in Commodities & Trade Finance: A Practical Guide” provides an overview of the general terms of the standard form of transactional commodities finance intercreditor agreement.⁶¹ In that article, I note that:

“Pursuant to (i) Section 9-312(d)(1)⁶² of the Uniform Commercial Code, as adopted in the State of New York (the “U.C.C.”), a security

⁵⁸ “Specific Security Interest” is defined to mean:

[A] perfected and enforceable security interest of a Creditor in any of the following Collateral, including the products and proceeds thereof and accessions thereto:

- (a) Collateral in the possession of the Creditor (or an agent or bailee on its behalf); or
- (b) Collateral made available to the Debtor by the Creditor (or its agent or bailee) pursuant to a trust receipt or other security agreement the effect of which is to create and/or continue the Creditor’s security interest therein, or the acquisition of which by the Debtor is enabled by any loan, documentary or standby letter of credit or other facility extended or issued by the Creditor to or for the account of the Debtor; or
- (c) Collateral covered by a non-negotiable document issued in the name of the Creditor or as to which the Creditor (or an agent or bailee on its behalf) controls possession through a negotiable document; or
- (d) Collateral which is an obligation owed by the Creditor to the Debtor; or
- (e) Collateral which is specifically identified in a Security Agreement, or in another writing, delivered to the Creditor at or about the time the security interest attaches.

See Lahny, *supra* note 6, at 386-387.

⁵⁹ See generally Lahny, *supra* note 6.

⁶⁰ See Lahny, *supra* note 6, at 388.

⁶¹ See generally Lahny, *supra* note 6.

⁶² Section 9-312(d)(1) of the U.C.C. states “While goods are in the possession of a bailee that has issued a nonnegotiable document covering the goods, a security interest in the goods may be

interest in goods in the possession of a bailee that has issued a non-negotiable document covering the goods, may be perfected by a non-negotiable document of title issued in the name of a secured creditor, and (ii) Section 9-313(a)⁶³ of the U.C.C., a security interest in goods in the possession of a bailee that has issued a tangible negotiable document covering the goods, may be perfected by a secured creditor taking possession of the tangible negotiable document.”⁶⁴

As further noted in that article, “with respect to goods covered by negotiable and non-negotiable documents of title, this provision seeks to align the priorities under the Form of Transactional Intercreditor Agreement with the priorities set forth in the U.C.C.”⁶⁵

However, since sea waybills are not documents of title, the underlying goods would not be covered by the same Specific Security Interest that would apply to goods covered by bills of lading.⁶⁶ Therefore, in addition to not having legal title to the underlying goods, the secured creditor would need to find a way for those goods to be covered under a different category of the definition of “Specific Security Interest,” in order to have a security interest that is senior to the other secured creditors that are party to the transactional commodities finance intercreditor agreement.⁶⁷

The good news for the applicable secured creditor is that if the underlying goods are covered by a sea waybill, absent fraud, no other secured creditor would have possession of bills of lading covering the same goods. Accordingly, pursuant to the terms of the transactional commodities finance intercreditor agreement, to the extent that the secured creditor actually financed the acquisition of the underlying goods, the secured creditor would have the senior Specific Security Interest under paragraph (b) of the definition of “Specific Security Interest.”⁶⁸ Pursuant to the terms of the transactional commodities finance intercreditor agreement, absent a secured creditor maintaining a Specific Security Interest under paragraph (c) (in respect of bills of lading), a

perfected by . . . (1) issuance of a document in the name of the secured party.” U.C.C. § 9-312(d)(1).

⁶³ Section 9-313(a) of the U.C.C. states “. . . a secured party may perfect a security interest in tangible negotiable documents, goods, instruments, money, or tangible chattel paper by taking possession of the collateral.” U.C.C. § 9-313(a).

⁶⁴ See Lahny, *supra* note 6, at 388.

⁶⁵ See Lahny, *supra* note 6, at 388-389.

⁶⁶ See generally Lahny, *supra* note 6.

⁶⁷ See generally Lahny, *supra* note 6.

⁶⁸ See Lahny, *supra* note 6, at 393-395.

secured creditor maintaining a Specific Security Interest under paragraph (b) of the definition of “Specific Security Interest,” would have the most senior Specific Security Interest in those underlying goods.⁶⁹ Therefore, actually financing the purchase of the goods will allow the secured creditor to maintain the senior Specific Security Interest in respect of such goods.

D. Potential Fraud Risk Associated with Sea Waybills

Another risk that arises in connection with the use of sea waybills is the risk that a fraudster impersonating the consignee could come to claim the goods.⁷⁰ As discussed above, due to the fact that sea waybills are not documents of title, to receive the underlying goods, the consignee does not need to produce any originals.⁷¹ The consignee is merely required to prove that he/she is the party named in the sea waybill.⁷² In addition, since sea waybills are non-negotiable, in nearly all cases, only the named consignee is able to retrieve the goods.⁷³

This creates a situation that can be rife with fraud. To the extent that the fraudster is aware of the company that is purchasing the applicable goods, producing documentation that indicates that the fraudster represents that company can be deceptively easy. Combined with the removal of the requirement to produce original documents, this does seem to increase the potential for this type of fraud.⁷⁴ That said, these types of typical fraud risks are always present during the shipping process and can easily be mitigated by the borrower being diligent in the offloading process.⁷⁵

* * *

Editor’s note: This article will conclude in the next issue of *The Banking Law Journal*.

⁶⁹ See Lahny, *supra* note 6, at 393-395.

⁷⁰ See Guidelines for the Release of Cargoes, International Transport Intermediaries Club Ltd. (2020).

⁷¹ See Williams, *supra* note 8, at 566.

⁷² See Williams, *supra* note 8, at 566; see also Ziakas, *supra* note 9 at 14.

⁷³ See Ziakas, *supra* note 9 at 14.

⁷⁴ See Guidelines for the Release of Cargoes, *supra* note 70.

⁷⁵ *Id.*