**KEY POINTS**

- English law is leading the way in the adoption of solutions to facilitate the digitisation of trade.
- The *possession problem* meant that physical possession of the document was preventing the trade and trade finance industry moving into the digital era.
- The Electronic Trade Documents Act 2023 (the Act) does not give a definitive list of documents which will be considered to be *electronic trade documents* having the same effect as the equivalent paper trade documents, yet it permits flexibility for the future.
- It is the functionality of the *reliable system* to achieve the legal status which is key to establishing an electronic trade document under the Act.



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# The Electronic Trade Documents Act 2023: the key to the future?

"Trade finance has continued to show its resilience and its ability to reinvent itself and to innovate. More players than ever are involved in different aspects of trade finance."[1]

Innovation is evidence of how trade and trade finance are developing in the international markets with the use of electronic platforms and technology which is constantly changing and improving. Internationally, the law, generally, has been trailing behind commerce and applications for trade. The coming into force of the Electronic Trade Documents Act 2023 (the Act) on 20 September 2023 is the key to legal recognition for certain electronic trade documents under English law. The Act, which is a very short piece of legislation, gives certain documents used in trade and trade finance the same legal status and protection as the equivalent documents in paper form. This article looks at some areas of the Act and the effect of the Act in the context of trade and trade finance.

## WHAT IS THE ISSUE THE ACT AIMS TO SOLVE AND WHAT WAS THE IMPETUS FOR THE CHANGE?

The impetus for the Act followed the publication of the UNCITRAL Model Law on Electronic Transferable Records (MLETR) which has now been adopted by upwards of seven countries with more to follow. With the international push to relieve trade and trade finance of some of the legal obstacles to save time, save paper, improve security, increase efficiency and create transparency, the Law Commission for England and Wales set up a consultation, and in March 2022 produced its *Electronic trade documents: Report and Bill* (the Report).[2] Using an expedited legislative route, the Electronic Trade Documents Bill was introduced to Parliament and promptly moved through to receiving Royal Assent on 20 June 2023. The decision not to adopt MLETR in the UK, meant the Act[3] focuses particularly on the one area of English law which was blocking the process for electronic trade documents being recognised and protected, before the Act came into force – the requirement of "possession".

"The problem that prevents the widespread digitalisation of these documents is that the law of England and Wales – like that of many other significant trade jurisdictions around the world – does not recognise intangible things as being amenable to possession."[4]

What is meant by "possession"? English law requires physical possession, whether actual or constructive, of certain documents to enable the holder to claim performance of the obligation set out in the document. There is a distinction between "title" or "ownership" and "possession" or holding a document.

For trade finance transactions this is often seen in promissory notes and bills of exchange under the Bills of Exchange Act 1882. In the context of trade, bills of lading are required for cargo onboard a vessel. They are also required for financing a transaction and taking security over the goods and documentation relating to them. The purchaser of the same goods will also need to have the bill of lading to be able to unload the goods at the destination port.

Similarly, warehouse receipts, issued on delivery of tangible goods to a warehouse, are needed in physical form to access the goods and retrieve them from the warehouse at a later date. In a pledge over tangible goods, the title to the goods is split from the concept of possession, so the secured creditor will have possession of the document with the right of sale, but the pledgor will retain rights to the goods so that it can sell them.

The "possession problem" meant that physical possession of the document required by legislation, common law or business practices was preventing the trade and trade finance industry moving into the digital era where speed and reduction of paper documents was, and is, becoming essential.

## WHICH TRADE AND TRADE FINANCE DOCUMENTS HAVE PROTECTION OF THE ACT?

The Act does not give a definitive list of documents which will be considered to be "electronic trade documents" having the same effect as the equivalent paper trade documents[5] within the terms of the Act. The documents in scope have to be used in "(i) trade in or transport of goods, or (ii) financing such trade or transport". The wording in the Act is slightly different to that of the draft Bill (which did include a specific list of documents in scope), in that it gives "examples of documents that are commonly used" for trade and trade finance.[6] These fall roughly into three camps:

- **documents used for payment**: bills of exchange and promissory notes;
- **documents used for trade and cargo**: bills of lading; ship's delivery orders; warehouse receipts and mate's receipts; and
- **certain insurance documents**: marine insurance policies and cargo insurance certificates.

This brings with it flexibility under English law, so that as commerce develops, other documents could fall within the protection of the Act. Indeed, other documents were tabled during the consultation stage when mate's receipts were added to the list, however, air waybills, sea waybills and freight forwarder's certificates did not appear in the final wording of the Act. So, in practice, to take advantage of the Act using other trade documents, it seems the burden would fall on the person trying to rely on the terms of the Act to show that the trade document being used in electronic form is of a type which would fall within scope, even if it is not listed in s 1 of the Act.

The scope is, however, limited and there are certain excluded documents set out in s 5 of the Act.[7] This leaves the matter to the interpretation of the English courts and the development of common law as cases are brought before them on the issue of whether a particular trade, transport or trade finance document not necessarily listed as an example in s 1 of the Act, is within scope. Furthermore, the Act does not make any particular statement about trade documents issued outside the UK and whether they will be covered or not. The Law Commission did look into this point and concluded in the Report[8] that it was not necessary, as there is "no rule that we are aware of to suggest that the law of England and Wales would deny recognition of a document simply because it was issued abroad".

## WHAT IS A "QUALIFYING ELECTRONIC TRADE DOCUMENT"?

To achieve the status of a "qualifying electronic trade document" under the Act, the document has to be a "trade document" and information related to it has to be on, and be used in, a "reliable system". The Act sets out guidance to identify a "reliable system"[9] and the five key actions[10] which the reliable system must be able to do. During the consultation, there was much discussion around the issue of "control" (meaning exclusive control) and concerns about fraud. The Act is not aimed at fraud or fraud prevention as this is dealt with by existing and imminent legislation.[11] "Control" however, is key and although there is no specific meaning in the Act, it does state that "a person exercises control of a document when the person uses, transfers or otherwise disposes of the document (whether or not the person has a legal right to do so)".[12]

A reliable system relates to the use of private keys (or any equivalent) to issue, transfer and amend a trade document in electronic form. Looking at this in the context of a trade or trade finance transaction, this does not mean accessing and reading a document, but it does mean creating, transferring, indorsing and disposing of a document. For granting security over any document in a reliable system, as well as granting the security in the form of a security document, eg a pledge, it will include in practice the electronic transfer of the document from the pledgor to a secured creditor, pending repayment of any outstanding facilities.

## WHAT DOES THE ACT REQUIRE A "RELIABLE SYSTEM" TO DO?

The Act sets out considerations or guidance on what a system needs to be able to do which is key as to whether the system can qualify as a "reliable system". To be a "reliable system" it should:

> "(a) identify the document so that it can be distinguished from any copies,
> (b) protect the document against unauthorised alteration,
> (c) secure that it is not possible for more than one person to exercise control of the document at any one time,
> (d) allow any person who is able to exercise control of the document to demonstrate that the person is able to do so, and
> (e) secure that a transfer of the document has effect to deprive any person who was able to exercise control of the document immediately before the transfer of the ability to do so (unless the person is able to exercise control by virtue of being a transferee)."

The aim of these provisions is to protect the "integrity" of the electronic document. The document could be issued outside the system and then uploaded to it. From that point, it needs to be identified as the original and not a copy such as an emailed pdf. For a holder in possession to be able to exercise the rights under it, including a right to payment or delivery of goods, the holder has to ensure that it is holding the *original* bill of exchange or promissory note or bill of lading or warehouse receipt as issued and not amended either by mistake or fraudulently without authority.[13] The concepts of access, control and disposal[14] aim to recreate the physical position of paper trade documents where one person "holds" the document, whether that is the holder or secured creditor, and only that person can transfer or dispose of it.

*One person* having "control" over the document is key to establishing a "qualifying electronic trade document" so that it is equivalent to the position with paper documents. A transfer must mean that the transferor will no longer have any control over that document and not have rights to then use, amend or transfer the document further. In other words, the transferor will "divest" itself of the rights in, and use of, the electronic document.

To aid transparency, it must be visible within the system who is the holder or who has exclusive control of the electronic document at any one time. While it was acknowledged in discussions with the Law Commission that the operator of the system may need to access the document to assist with any technology glitches, this would not give the operator any legal rights over the documents,[15] however, there is no specific exception for the operator as such. The Act does not go into detail on technology requirements as these may change from time to time and from system to system. It is the functionality of the system being used to achieve the legal status which is key to establishing an electronic trade document under the Act.

## HOW CAN AN OPERATOR DETERMINE IF IT HAS A "RELIABLE SYSTEM"?

While the Act sets out the five specific requirements for the "qualifying electronic trade document", it leaves the definition of "reliable system" open to more flexible interpretation by providing a list of considerations which "may be taken into account".[16] As the requirements are not prescriptive, this is intended to leave room for development of technology still in the testing phase or for new methods of working with systems or even across systems on an inter-operable set of systems.

The issue for those wanting to use the provisions of the Act, inevitably will be who has the burden of proof in any dispute that they have the protection of the Act because the system being used is a "reliable system". Will it be the seller, the buyer of goods or the payment obligation, the financier or the operator who finds themselves before the court bringing in extrinsic evidence to back up their argument to fall within the

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scope of the Act? Could parties agree amongst themselves that they are satisfied that the system is a reliable system within the scope of the Act? Much is, as yet, open to interpretation.

The Act is, therefore, technology neutral. There is no requirement that each of the seven considerations listed needs to be met. However, it is currently an issue for the trade and trade finance industry as to how to demonstrate to those wanting to take advantage of the Act, that the operator does in fact have a "reliable system" within the terms of the Act.[17]

Some of the considerations[18](a-d) are likely to be areas a business might expect to see with any online business or system it is contracting with, eg integrity, security of the hardware and software, security of the information, rules of the system and measures to prevent unauthorised access. The considerations in paragraphs (e-f): "(e) regularity of and extent of any audit of the system by an independent body; (f) any assessment of the reliability of the system made by a body with supervisory or regulatory functions", do seem to be raising concerns that in practice may be requiring users to add additional layers of checks and evidence which might delay the use of some systems until an audit, certification or approval, and from whom, is issued for a system to give it a quality mark of some description as a "reliable system". This is not a legal requirement to qualify under the Act but seems to be emerging as a possible user requirement. Bodies including the ICC (International Chamber of Commerce) and ITFA (International Trade and Forfaiting Association) are involved in these discussions.

## IMPLEMENTATION AND USE OF THE ACT

Much of the detail on implementation has been left to users. Industry standards and voluntary codes of conduct are likely to play a part in how, and the extent to which, the trade and trade finance industry adopt the Act and the use of electronic trade documents after 20 September 2023. The Act has two functions, to clear the English law "blocker on possession" and to facilitate the use of electronic trade documents.

English law, together with the legislation already adopted in the countries which have adopted MLETR and future legislation along the lines of the Act and MLETR being considered, and once adopted in other G7 states, will open up the possibility of using bills of exchange, promissory notes, bills of lading and warehouse receipts and other trade documents in electronic form worldwide.

In the wider context, the Act assumes co-operation between the various parties to a transaction (seller, buyer, transporter, financier(s), secured creditor and, of necessity, port authority or warehouse operator) as users with access to the same or an equivalent reliable system. Will they each, in whatever part of the world they are based, have the internet coverage, hardware, the data storage needed and skilled staff to function as an issuer, user, financier, secured creditor, holder or operator of, or in, a reliable system? Would a party have to consider joining several systems to access the benefits of the Act? Whether that would be cost effective will remain a matter for each party and operator. Solutions should be designed to simplify the access to any applicable reliable system at the time needed to access the relevant electronic trade document.

The Act is, however, set in reality and recognises that in the real world developments will occur at different times in different locations and so it allows a trade document originally in paper form to be converted into electronic form, and for a document in electronic form to be converted into paper form.[19] To make sure that there is no abuse of this right and to avoid duplication of the trade document, the document once converted should include "a statement that the document has been converted" into its new form. Consequently, the original document in its previous state will cease to have any effect.

Developments on interoperability of reliable systems will be left to users and the sectors within them (eg shipping, banking, agriculture and the transport sector) to find workable, efficient technology solutions which can take advantage of the use of electronic trade documents.

What seems certain is that English law is leading the way in the adoption of solutions to facilitate the digitisation of trade. ■

*Disclaimer*: The material in this article is for general information only and is not legal advice. No liability is accepted for any loss or damage which may result from reliance on it. Always consult a qualified lawyer about a specific legal issue.

1 *A Practitioner's Guide to Trade and Commodity Finance.*
2 Law Commission No 405. Sullivan & Worcester UK LLP responded to the consultation and were quoted in the Report.
3 The draft Bill was only expected to apply to England and Wales; however, the Act also applies to Scotland and Northern Ireland. Issues of personal property are devolved issues for Scotland and the Act contains provisions relating to the Scottish Ministers as well as the Secretary of State. Section 3(4) only applies to Scotland because of the categorisation of property under Scots law.
4 Law Commission 405 at p 13 and *OBG Ltd v Allan* [2001] UKHL 21.
5 Section 3(2) of the Act.
6 Section 1(2) of the Act.
7 (a) an uncertificated unit of a security that is transferable by means of a relevant system in accordance with the Uncertificated Securities Regulations 2001 (SI2001/3755); or (b) a document or instrument of a type specified in regulations made by the appropriate authority.
8 Law Commission No 405 para 8.116.
9 Section 2(5).
10 Section 2(2).
11 Fraud Act 2006 and on other legislation on financial crime. The UK government is proposing legislation on the prevention of fraud, at the time of writing.
12 Section 2(3)(a).
13 (a) and (b).
14 Set out in (c-e).
15 Section 2(4).
16 Section 2(5).
17 See ICC and C4DTI – the Centre for Digital Trade & Innovation for more information.
18 Section 2(5).
19 Section 4.

*Further Reading:*

- Electronic trade documents: a way forward? (2021) 7 JIBFL 497.
- A roadmap for legal reform: the future UNCITRAL/UNIDROIT Model Law on Warehouse Receipts (2023) 8 JIBFL 553.
- Lexis+® UK: Banking & Finance: News: Electronic Trade Documents Act – paper to data.