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REPORT ON LETTERS OF TRUST BY Mr. GUTTERIDGE

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The letter of trust is an expedient which is in common use in Great Britain and the United States in connection with agreements by which the price of imported goods is to be paid by a banker who issues a letter of credit in favour of the seller for that purpose. In such cases the documents of title to the goods are retained by the banker as security for the reimbursement of the monies which he advances to the importer, and a situation frequently arises in which it would be advantageous both to the financing banker and the importer that the importer should warehouse the goods on arrival and should sell them and deliver them in his own name to the ultimate buyer. The difficulty is that if this is done and the documents of title are surrendered to the importer by the banker for that purpose, the security of the banker which is dependent on possession of the documents ceases to be effective in law.

The procedure by way of letter of trust has been adopted in order to meet this difficulty, and to enable the banker to give possession of the goods or of the documents of title to his customers, the importer, for the purpose of facilitating the warehousing or sale of the goods, and at the same time to retain his security unimpaired.

The procedure adopted is broadly speaking as follows. On arrival of the goods the banker hands the documents to the importer in exchange for the letter of trust. This is a letter signed by the importer and addressed to the banker which is usually expressed in the following terms:

"I undertake to hold the documents of title and the goods when received and the proceeds thereof when sold as trustees for the bank⁽¹⁾.

- A) As I require the said documents in order to obtain delivery of the goods⁽²⁾ I undertake to warehouse them in the name of the bank and to hand the warrants to the bank forthwith; also to insure the goods against fire to their full insurable value and to hold the policies on behalf of the bank and in case of loss to pay the insurance monies to the bank.
- B) As I require the said documents in order to deliver the goods⁽²⁾ to the buyer I undertake to pay the proceeds of sale to the bank without deduction immediately on receipt thereof within..... days from this date and to furnish the bank on request with full authority to receive the purchase price from any person or persons. In the meantime I undertake to hold the goods on trust for the bank⁽³⁾. The bank may at any time cancel this letter and take possession of the goods until they have been delivered to the purchasers and the price has been received from them and may collect the price if the same has not been paid by the purchasers".

(1) Although the word "trust" is used in this connection this is technically inaccurate as the transaction is not the creation of a trust. See Gutteridge, Banker's Commercial Credits, p. 75; also Frederick, The Trust Receipt as Security, a brochure published by the American Acceptance Council.

(2) A and B are alternative and one or other will apply according as it is desired either that the importer should merely warehouse the goods or that he should deliver them to the ultimate buyer.

(3) The importer is sometimes required to declare that he is not indebted to the ~~importer~~^{seller} of the goods.

Letters of trust in this form have been treated as valid by the Courts of law in Great Britain and the United States though the juridical basis of such recognition is still a matter of some uncertainty⁽¹⁾. An importer who has signed a letter of trust and deals fraudulently with the goods also commits a crime for which he can be punished. It is believed that letters of trust in a modified form are in use at Le Havre in connection with the importation of grain, sugar and tobacco, though only to a limited extent because their validity is doubtful according to French law. We have also been informed that documents of this nature are employed in Germany, but have no information before us as to their exact nature or as to their validity in German law. In Great Britain and the United States they operate not merely to keep the banker's security in existence, notwithstanding the fact that he has parted with the documents, but they also enable the banker to enforce such security as against the other creditors of the importer in the event of his insolvency. They are ineffective, however, against the claims of a purchaser who has received the goods and paid the price without notice of the existence of a letter of trust.

Although they are chiefly used in connection with the importation of goods from abroad they are sometimes used in the United States, but not in Great Britain, in connection with domestic transactions, e.g., the sale of automobiles.

(1) See Gutteridge, op. cit., Frederick, op. cit.
The Committee were also informed that they have been recognised as valid by the Brazilian Courts.

That letters of trust serve a valuable purpose in international commerce cannot be doubted. They relieve bankers of the trouble and expense of warehousing the goods on arrival and they enable the goods to be marketed by the person who is, as a rule, best able to sell them to advantage, i.e., the importer, without causing the loss of commercial prestige which might result if it was apparent that he was trading with borrowed funds. It seems that they would be utilised to a wide extent if their validity was admitted by all systems of law. The question of the legal recognition of letters of trust is one which, in our opinion, calls for serious and immediate consideration from an international point of view. It would be a misfortune if the matter is left to be dealt with by isolated action on the part of the countries concerned. This would lead to a regrettable diversity of laws which we think can be avoided if an effort is made now to secure the co-ordination of legislation on the question.

We do not, however, consider that the international code of the law of sale should deal with this transaction, which is of a somewhat special character. In any event any attempt on our part to frame international rules governing letters of trust would, in our opinion, be premature, as the legal problems involved call for careful study in their relation to the rules of the different systems of law which are concerned. So far as it is possible, at present, to envisage the nature of these problems the difficulties which will be encountered are the following:

- 1 - The banker must be vested with property in the documents which will be adequate in order to enable him to control the sale of the goods until such time as his claims are satisfied by the importer;

2 - His right of property must not be destroyed by the surrender of the documents to the importer;

3 - He must be protected, in the event of the importer's insolvency, against claims by the general body of creditors.

The matter is also one which must be explored in its relation to the business practice of bankers throughout the world and regard must no doubt also be had to other economic aspects of the question.

We, therefore, confine ourselves to addressing an invitation to the Council to take such steps as they may consider to be advisable for the purpose.