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OF LETTERS OF INDEMNITY AND "SPENT" BILLS OF LADING

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I. Introduction

1 From a survey of Singapore case law spanning the last two decades or so, it would appear that the issue of whether a bill of lading is "spent" has arisen in only a handful of cases. This article discusses three of them: *BNP Paribas v Bandung Shipping Pte Ltd*[1] ("*BNP Paribas*"), *The Dolphina*[2] and, most recently, *The Yue You 902.*[3] In *BNP Paribas* and *The Yue You 902*, Belinda Ang Saw Ean J and Pang Khang Chau JC, respectively, decided that the bills of lading in question were not "spent". In *The Dolphina*, Ang J held that it was not necessary to decide the issue, although Her Honour commented that it could be considered a complex issue.[4]

2 A common thread running through all three cases is that the shipowner delivered the cargo against a letter of indemnity instead of against the production of the relevant original bill of lading; and this became the source of the shipowner's woes.

3 Given this common thread, it would be useful to first discuss the risks a shipowner is exposed to when it agrees to release cargo without the production of the original bill of lading.

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* The author would like to thank his colleague S Mohan for his comments on the draft of this article. Any error is solely the author's.

1 [2003] 3 SLR(R) 611. See paras 20–23 below.

2 [2012] 1 SLR 992. See paras 32–37 below.

3 [2019] SGHC 106. See paras 24–31 below.

4 *The Dolphina* [2012] 1 SLR 992 at [181].

II. Letters of indemnity

4 In a usual conveyance of goods, when a cargo is loaded onboard a vessel, the shipowner will normally issue a bill of lading to the party shipping the cargo (the "shipper") to acknowledge receipt of the cargo on the terms set out in the bill of lading. The shipper will then transfer the bill of lading to the party receiving the cargo at the discharge port (the "consignee"). When the vessel arrives at the discharge port, the consignee, who would have received the bill of lading in the meantime, presents the bill of lading to the shipowner to collect the cargo. Where a bank (or some other lender) has financed the sale and purchase of the goods, instead of transferring the bill of lading directly to the consignee, the shipper (as the seller) will transfer the bill of lading to the bank in exchange for payment for the goods. Thereafter, the bank will only transfer the bill of lading to the consignee (as the buyer) after the consignee has paid for or, often times, obtained a loan from the bank to pay for the goods.

5 A bill of lading has three main functions: (a) it acts as a *document of title*; (b) it is a *receipt* for the goods shipped onboard the vessel; and (c) when in the hands of a person other than a charterer, it contains or is evidence of the terms of the contract of carriage between the owner and the holder of the bill of lading.

6 The usual practice is for bills of lading to be issued in a set of three originals – one for the shipper, one for the bank and one for the consignee. Because they are issued in a set of three originals, a bill of lading would invariably contain the following clause (usually printed on the face of the bill of lading) or some other similarly worded clause:[5]

> In witness whereof the Master has signed three Bills of Lading of this tenor and date, one of which being accomplished, the other is void.

5 See the example in *The Dolphina* [2012] 1 SLR 992 at [137].

7 It has been consistently held by the courts[6] that such a clause obliges the shipowner to deliver cargo to the lawful holder of the bill of lading, upon the presentation of any one of the three original bills of lading in a set; this has been referred to as the "presentation rule".[7] It is because of the existence of the presentation rule that a bill of lading can function as a document of title so that the transfer of the bill of lading also transfers the right (to the lawful holder of the bill of lading) to demand the cargo from the ship at discharge.[8]

8 A shipowner who does not comply with the presentation rule may be liable for conversion and breach of contract. Indeed, it has also been held that because under a bill of lading contract a shipowner is obliged to deliver goods upon production of the original bill of lading, delivery without the production of the bill of lading constitutes a breach of contract even when made to the person entitled to possession of the cargo.[9]

9 Some charterparties (especially charterparties used for the transportation of oil cargo) contain provisions which provide that in the absence of the original bills of lading at the discharge port, the shipowner is to discharge and release the cargo to the consignee against a letter of indemnity (usually furnished by the charterers).[10] The courts have consistently held that such a clause (sometimes referred to as an "letter of indemnity clause") does not permit or legitimise the delivery of cargo without the production of the original bill of lading, but merely entitles the shipowner to an indemnity for any liability that he may be

6 *BNP Paribas v Bandung Shipping Pte Ltd* [2003] 3 SLR(R) 611 at [26]; *The Dolphina* [2012] 1 SLR 992 at [152]; *The Yue You 902* [2019] SGHC 106 at [24].

7 *The Dolphina* [2012] 1 SLR 992 at [137]–[143].

8 *The Dolphina* [2012] 1 SLR 992 at [140], citing the comments of Neill LJ in *Kuwait Petroleum Corporation v I & D Oil Carriers Ltd* (*The Houda*) [1994] 2 LR 541.

9 *The Dolphina* [2012] 1 SLR 992 at [141], citing the comments of Leggatt LJ in *Kuwait Petroleum Corporation v I & D Oil Carriers Ltd* (*The Houda*) [1994] 2 LR 541 at 553. The correctness of this position appears to have been doubted by Pang JC in *The Yue You 902* [2019] SGHC 106 at [69].

10 An example of the usual terms in such a letter of indemnity can be found in *The Dolphina* [2012] 1 SLR 992 at [33].

exposed to should he choose to do so.[11] As Leggatt LJ succinctly put it in *The Houda*:[12]

> In default of production of the bill of lading an indemnity is afforded to the shipowner not on account of the lawfulness of the order to deliver but so as to protect him if he does what he is *not* contractually obliged to do. [emphasis in original]

10 It is precisely because delivery without production of the original bill of lading constitutes a breach of contract that most (if not all) shipowners will invariably insist on receiving a letter of indemnity, indemnifying the shipowner for any liability he may be exposed to as a result of breaching the bill of lading contract, before agreeing to release the cargo without the production of the original bill of lading.

11 Indeed, as a result of the prevalence of the practice of delivering cargo against a letter of indemnity, the International Group of Protection and Indemnity Clubs has produced two standard form letters of indemnity – the A form and the AA form (the latter form is used when a bank agrees to also be a party to the letter of indemnity) – which its shipowner member(s) are recommended to obtain when agreeing to deliver cargo without the production of the original bill of lading. It must be said, however, that a misdelivery claim (brought by the lawful holder of the bill of lading against the shipowner) arising from delivery without production of bill of lading is a discretionary claim under a shipowner's protection and indemnity policy ("P&I"), and the P&I insurer may well decline cover for such a claim.[13]

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11 *BNP Paribas v Bandung Shipping Pte Ltd* [2003] 3 SLR(R) 611 at [65]–[69], and cited with approval by Pang JC in *The Yue You 902* [2019] SGHC 106 at [84]–[85].

12 *The Dolphina* [2012] 1 SLR 992 at [148], citing Leggatt LJ in *Kuwait Petroleum Corporation v I & D Oil Carriers Ltd* (*The Houda*) [1994] 2 LR 541 at 553.

13 See, for example, r 19(17)(e)(D) of the North of England Club's P&I Rules (2019–20), which states:

> ...
> unless the Members Board in the exercise of its discretion shall otherwise determine no claim on the Association shall be allowed in respect of a Member's liability arising out of:
>
> ...

(*cont'd on the next page*)

12 That aside, a letter of indemnity is only worth as much as the creditworthiness of the indemnitor (*ie*, the party who issued the letter of indemnity). An indemnitor that does not have sufficient assets to meet its liability under the letter of indemnity when called upon to do so, or worse still, has become insolvent by that time, will provide scant comfort to the shipowner.

13 Moreover, a letter of indemnity would generally be limited to a certain amount (often 100% of the cost, insurance and freight value of the cargo) because an indemnitor would not agree to be exposed to unlimited liability under the letter of indemnity. As such, it is possible for the shipowner to be under-secured because the shipowner's liability may well exceed the limit under the letter of indemnity (for example, on account of consequential damages). Also, a letter of indemnity is usually valid only for a fixed period. The shipowner may be left exposed if a claim is only made against him by a bill of lading holder after the letter of indemnity has expired.

14 When a shipowner is faced with a misdelivery claim, but is unable to pass on the claim to his P&I insurer or obtain an indemnity under the letter of indemnity, it would not be surprising for the shipowner to resist the claim by challenging, amongst others, the claimant's title to sue under the bill of lading – this is when the issue of whether the bill of lading is "spent" at the time when the holder came into possession of it, comes to the forefront.

> (iii) delivery of cargo carried under a negotiable bill of lading or similar document of title (including an electronic bill of lading) without production (or the equivalent thereof in the case of an electronic bill of lading) of that bill of lading or document by the person to whom delivery is made (unless in the case of an electronic bill of lading there has been proper delivery to the person so entitled in accordance with the terms of an electronic trading system approved pursuant to Proviso (I) of this Rule);
>
> ...

III. Transfer of rights of suit under a bill of lading

15 Section 2(1)(*a*) of the Bills of Lading Act ("Act") provides:[14]

> 2.—(1) Subject to the following provisions of this section, a person who becomes —
>
> (*a*) the *lawful holder* of a bill of lading ...
>
> shall (by virtue of becoming the holder of the bill of lading ...) have transferred to and vested in him all *rights of suit* under the contract of carriage as if he had been a party to that contract.
>
> [emphasis added]

16 Section 2(2) of the Act provides:

> (2) Where, when a person becomes the lawful holder of a bill of lading, *possession of the bill no longer gives a right (as against the carrier) to possession of the goods to which the bill relates*, that person *shall not have any rights transferred to him* by virtue of subsection (1) *unless* he becomes the holder of the bill —
>
> (*a*) by virtue of a transaction effected in pursuance of any contractual or other arrangements made before the time when such a right to possession ceased to attach to possession of the bill; or
>
> (*b*) as a result of the rejection to that person by another person of goods or documents delivered to the other person in pursuance of any such arrangements.
>
> [emphasis added]

17 As explained in *The Yue You 902*,[15] s 2(1) of the Act decoupled the transfer of rights of suit from the passing of property, whilst s 2(2) of the Act addressed the concern that decoupling the transfer of rights of suit from passing of property would lead to potentially undesirable transfer of rights of suit after a bill of lading is spent. Section 2(2) seeks to address this by

14 Cap 384, 1994 Rev Ed.

15 [2019] SGHC 106 at [35]–[36].

imposing restrictions on the transfer of rights of suit in relation to spent bills.

18 The term "lawful holder" is defined in s 5(2) of the Act as follows:

> (2) References in this Act to the holder of a bill of lading are references to any of the following persons:
>
> > (*a*) a person with possession of the bill who, by virtue of being the person identified in the bill, is the consignee of the goods to which the bill relates;
> >
> > (*b*) a person with possession of the bill as a result of the completion, by delivery of the bill, of any indorsement of the bill or, in the case of a bearer bill, of any other transfer of the bill;
> >
> > (*c*) a person with possession of the bill as a result of any transaction by virtue of which he would have become a holder falling within paragraph (*a*) or (*b*) had not the transaction been effected at a time when possession of the bill no longer gave a right (as against the carrier) to possession of the goods to which the bill relates,
>
> and a person shall be regarded for the purposes of this Act as having become the lawful holder of a bill of lading wherever he has become the holder of the bill in good faith.

19 A bill of lading is said to be "spent" or "accomplished"[16] once the goods, in respect of which the bill of lading was issued, have been delivered to the person entitled to them. A spent bill of lading is "no longer an effective document of title that enables the constructive possession of the goods to be transferred by a transfer of the bill";[17] or in s 2(2) parlance, "possession of the bill no longer gives a right (as against the carrier) to possession of the goods to which the bill relates." However, a bill of lading is *not* spent if goods covered by it have been misdelivered to a party

16 Recalling the notation "one of which being accomplished, the others to stand void" commonly found on the face of a bill of lading.

17 Tan Lee Meng, *Law on Carriage of Goods by Sea* (Academy Publishing, 3rd Ed, 2018) at para 07.042.

not entitled to the goods;[18] arguments to the contrary have been rejected by the court.

A. BNP Paribas v Bandung Shipping Pte Ltd

20 In *BNP Paribas*, the plaintiff BNP financed the purchase of several parcels of palm oil and palm olein by its customer Shweta International Pte Ltd, which chartered the carrying vessel from the defendant. Shweta on-sold the cargo to Lanyard Foods Ltd. The cargo was released by the shipowner against a letter of indemnity issued by Lanyard, instead of against the production of original bills of lading. In the event, Lanyard took the goods but failed to pay for them and Shweta defaulted under the loan. The bills of lading were indorsed and delivered to BNP *after* the cargo had been discharged. When BNP demanded delivery under the bill of lading, it found that the goods had already been delivered to Lanyard.

21 Unsurprisingly, the shipowner argued that BNP did not acquire any rights of suit under the bills of lading because by the time BNP became the lawful holder of the bills, the bills had already been spent. Ang J rejected the argument and held that the bills of lading were not spent because the cargo had been delivered to persons who were *not* entitled to the cargo.[19]

22 Ang J further held that even if the bills were spent, BNP would still have acquired rights of suit because BNP had become the holder of the bills by virtue of a facility agreement that was established in July 1999, long before the cargo was (mis)delivered; s 2(2)(*a*) read with s 5(2)(*c*) would have been satisfied.

23 Given that BNP had the requisite title to sue, and the owners had failed to deliver the goods when called upon to do so by BNP, judgment was entered against the shipowner.

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18 *The Yue You 902* [2019] SGHC 106 at [44]–[45], following *BNP Paribas v Bandung Shipping Pte Ltd* [2003] 3 SLR(R) 611 at [30].

19 *BNP Paribas v Bandung Shipping Pte Ltd* [2003] 3 SLR(R) 611 at [30] and [50].

B. The Yue You 902

24 The facts in *The Yue You 902* were in several respects similar to those in *BNP Paribas*. The plaintiff, OCBC Bank, financed the purchase of cargo, which was shipped on the vessel in respect of which 14 sets of bills of lading were issued. The cargo was discharged against a letter of indemnity without the production of the original bills of lading. The receiver of the cargo failed to pay for the cargo and the bank was not repaid its loan. As the bank held the bills of lading as security, the bank presented the bills of lading to the shipowner and demanded delivery of the cargo. Needless to say, the shipowner was unable to deliver the cargo to the bank.

25 The bank had received the bills of lading *prior* to the commencement of discharge of the cargo, but only made payment for the cargo (pursuant to a trust receipt loan, which its customer had requested for *whilst* the cargo was being discharged) *after* the cargo had been fully discharged. The shipowner sought to argue that the bills of lading become spent once delivery has taken place even if it was not to a person entitled. The shipowner further contended that the "contractual or other arrangements" pursuant to which the bank becomes the lawful holder of the bills of lading was the granting of the trust receipt loan by the bank (*ie*, when the bank paid for the cargo).[20] It was argued that as this took place after the cargo had been fully discharged (at which time the bills were spent), the bank could not rely on s 2(2)(*a*) of the Act to acquire any rights of suit.

26 The argument (that a bill could become spent even if cargo was delivered to a person that was not entitled to the cargo) was roundly rejected by the court. Pang JC relied on *BNP Paribas* as well as other case authorities dating as far back as 1870.[21] Pang JC also clarified that the phrase "possession of the bill no longer gives a right (as against the carrier) to possession of the goods to which the bill relates" refers to the *document of*

20 As per s 2(2)(*a*) of the Bills of Lading Act (Cap 384, 1994 Rev Ed).

21 *The Yue You 902* [2019] SGHC 106 at [58]–[61].

title function of a bill of lading in transferring constructive possession of the goods to which the bill relates and covers the situation where a bill of lading would at common law be regarded as "spent".[22]

27 It would be recalled that the bank physically acquired the bills prior to commencement of discharge. As mentioned earlier, the shipowner argued that the "contractual or other arrangement" pursuant to which the bank had acquired the bills was the trust receipt loan (which was granted only after discharge had been completed). This argument was rejected. Pang JC held that the trust receipt loan was merely the "transaction" by virtue of which the bank acquired the bills; the preceding "contractual or other arrangement" pursuant to which the "transaction" was effected was, in fact, the facility agreement.[23] In other words, the "transaction" referred to the physical process by which the bill was transferred, whereas the "reason or cause" (or "the trigger") for the bills of lading being transferred from one person to another was the facility agreement.

28 The court emphasised that the "contractual or other arrangement" ought to be identified using a broad approach to causal connection. Indeed, Pang JC opined that the "contractual or other arrangement" need not even involve the claimant as a party to it.[24] In *BNP Paribas*, Ang J also held that the overarching facility agreement was the relevant "contractual or other arrangement" and not the trust receipt arrangement. This would suggest that it would not be difficult for a holder of a spent bill of lading to be able to bring itself within one of the exceptions that would still enable rights of suit to be acquired.

29 The shipowner's alternative defence that the bank was not a lawful holder (because it had allegedly acquiesced in the delivery without production of the original bills, by agreeing to a

22 That is, when the bill of lading is no longer effective as a document of title.

23 *The Yue You 902* [2019] SGHC 106 at [88].

24 *The Yue You 902* [2019] SGHC 106 at [95].

trust receipt arrangement) was also rejected; Ang J had also rejected a similar argument in *BNP Paribas*.[25] Pang JC reiterated the proposition that a person becomes a lawful holder of a bill of lading "in good faith" if he became its holder *honestly* and not where possession of the bill of lading was obtained unlawfully or by improper means. His Honour commented that a bank which receives a bill of lading from the banking chain (originating from a seller) can reasonably take the view that the bill is not a spent bill because even if cargo had been delivered, it would not have been to a person entitled to delivery because the bills of lading are with the bank.[26]

30 Given that a bill of lading will only be spent when cargo is delivered to a person entitled to delivery (and ordinarily) against presentation of the original bill of lading, the question may arise as to whether a spent bill could still be "trafficked" such as to render s 2(2) of the Act otiose. Usefully, Pang JC provided examples of situations where a spent bill of lading could still be trafficked:[27]

> (a) when only one bill (out of three) is presented for discharge, the other two bills could still be transferred or pledged separately from the bill that was presented;
>
> (b) cargo may be delivered by the shipowner upon *sight* of the original bill of lading without the original bill being *retained* by the shipowner;
>
> (c) the bill can be spent so long as cargo is delivered to the person entitled without the bill being sighted (let alone retained) by the owner; and
>
> (d) the person entitled may receive the goods before receiving the bill of lading; once he receives the bill of lading, it becomes spent. However, before that, he could (mis)use the bill knowing that it will become spent imminently.

25 *BNP Paribas v Bandung Shipping Pte Ltd* [2003] 3 SLR(R) 611 at [56]–[64].

26 *The Yue You 902* [2019] SGHC 106 at [115].

27 *The Yue You 902* [2019] SGHC 106 at [66]–[71].

31 In the event, Pang JC rejected all the arguments and defences raised by the shipowner and entered summary judgment.

C. The Dolphina

32 In *The Dolphina*, the buyer applied for and obtained a letter of credit from the plaintiff bank (in June) after the cargo had been fully discharged (in April) by relying on a sham contract of sale, which showed that the cargo was to be delivered in June and before 30 June. The cargo was discharged against a letter of indemnity issued by the seller/charterer, who obtained possession of and retained the bill of lading in April. To obtain payment under the letter of credit, the seller indorsed the bill of lading (in blank) in June – even though the cargo had already been delivered in April – and presented it as part of the documents required under the letter of credit. When the bank demanded delivery of the cargo, the shipowner was unable to effect delivery of the cargo.

33 Ang J was unequivocal that the shipowner was in breach of the bill of lading contract by delivering the cargo without the production of the original bill of lading against a letter of indemnity.[28] However, the issue of the bank's title to sue was hotly contested by the parties.

34 The bank's arguments were that it was a lawful holder of the bill of lading (which had been blank indorsed by the seller/charterer) and the bill of lading was not spent when it acquired possession of it; even if it was, the bank could rely on s 2(2)(*a*) of the Act to acquire rights of suit.[29]

35 The shipowners, on the other hand, argued that the bank never became the lawful holder as there was never an intention for the bank to be a holder because within hours of receiving the bill of lading, the bank relinquished the bill of lading to its

28 *The Dolphina* [2012] 1 SLR 992 at [134]–[142].
29 *The Dolphina* [2012] 1 SLR 992 at [156]–[157].

customer. Moreover, it was questionable whether the bank was a holder in good faith, given that when the letter of credit was opened in June, the bank knew that the cargo had already been shipped in March and that was why the bank allowed the letter of credit documents to be presented within 100 days from the date of shipment when the usual length permitted was around 21 days. The owners also argued that the cargo had been delivered to a person entitled to the cargo and thus spent.[30] The parties also disputed whether a bill would be spent if the cargo had been delivered to a person entitled to it, but who *did not* produce the original bill of lading.[31]

36 In the event, Ang J did not have to decide on any of these issues. Instead, Her Honour found that the indorsement of the bill by the seller was not a valid indorsement and, therefore, the bank could not be considered a holder (let alone a lawful holder) of the bill of lading who could acquire any rights of suit thereunder. Ang J held that where a claimant relies on s 5(2)(*b*) of the Act to establish that he is a holder of the bill because he is a "person with possession of the bill as a result of the completion, by delivery of the bill, of any indorsement of the bill", the indorsement of the bill had to be a *valid* indorsement. Her Honour held that even though s 5(2)(*b*) of the Act did not contain the word "valid", case law indicates that "any indorsement" must mean "any valid indorsement"; an indorsement which was in error is not an effective indorsement nor is an indorsement tainted by fraud.[32]

37 Ang J found that the seller's act of indorsing the bill of lading (in June), even though it knew that the cargo had already been delivered (in April), was fraudulent and was therefore not a valid indorsement.[33] As such, the bank did not acquire any rights

30 *The Dolphina* [2012] 1 SLR 992 at [158]–[159].

31 In *The Yue You 902* [2019] SGHC 106 at [19], Pang JC expressed the view that a bill would be spent when cargo was delivered to the person entitled even if the original bill of lading was not presented.

32 *The Dolphina* [2012] 1 SLR 992 at [165]–[172].

33 *The Dolphina* [2012] 1 SLR 992 at [173]–[179].

of suit under the bill. The bank, however, succeeded in its claim for conspiracy and obtained judgment for the value of the cargo.

IV. Conclusion

38 The three cases discussed above emphasise the following points that are of importance to persons dealing with bills of lading, especially shipowners and banks who finance the sale and purchase:

(a) A shipowner risks a claim for misdelivery when cargo is delivered, not against the original bill of lading, but against a letter of indemnity. A provision in the charterparty permitting the shipowner to deliver cargo against a letter of indemnity would not absolve the shipowner of liability.

(b) Even if a shipowner had procured a letter of indemnity, the shipowner could still be liable to the lawful holder of a bill of lading for the value of the cargo without being able to pass on the claim to his P&I insurer or obtain compensation under the letter of indemnity.

(c) To become a lawful holder of a bill of lading under the Bill of Lading Act, a person must acquire the bill of lading pursuant to a valid indorsement – an indorsement tainted by fraud is not a valid indorsement.

(d) A bill of lading will not be "spent" or "accomplished" unless delivery is made to the person entitled to the cargo. However, there are still situations where a spent bill of lading may be trafficked.

(e) Even when a lawful holder acquires a spent bill of lading, it can still obtain rights of suit so long as it acquired the bill pursuant to the contractual or other arrangements which were already in place before the bill became spent. The courts' inclination is to adopt a broad approach when identifying such an arrangement.

39 With the introduction of electronic bills of lading,[34] only an electronic copy of a bill of lading ("e-bill") will be generated when cargo is shipped onboard a vessel. It would be interesting to see how, in practice, an e-bill is to be "presented" or "indorsed". Presently, the Act does not expressly deal with the use of an e-bill. It can be envisaged that the law in this area will continue to evolve to cope with the digitalisation of what has all along been a paper document.

34 In 2019, the Infocomm Media Development Authority, the Maritime and Port Authority of Singapore, Singapore Customs and the Singapore Shipping Association embarked on an initiative, known as TradeTrust, to develop the digital infrastructure to promote the digitalisation of bills of lading. See Ministry of Communications and Information, "Trade Trust: A Trusted Global Network for Digitally Interconnected Trade Documents".