

# The Practicability of Farming Product Secured Credit in Ethiopia: Some Insights

Tajebe Getaneh Enyew\*

## *Abstract*

*Many countries in the world reform their secured transactions law on a movable property to unlock access to credit to their society. Recently, Ethiopia also reforms its movable property security right law by proclaiming a comprehensive Movable Property Security Rights Proclamation. This Proclamation provides an extensive list of movable properties that a debtor can grant to secure his obligation. Farming product is one category of movable property that the proclamation allows a debtor to use as collateral to secure the creditor's right. However, though the proclamation explicitly entitles debtors to grant their farming products as collateral, it is very doubtful whether it is going to be practicable. The purpose of this paper is, therefore, to assess the practicability of farming products secured credit in Ethiopia. In addressing this issue, the author adopts a qualitative research approach and typically doctrinal research type. The author uses data collected from legislation and pieces of literature through document analysis. After evaluating the issue from different perspectives, the author concludes that a secured credit backed by a farming product will face problems to be practiced as much as the proclamation intends. The author identifies three critical problems that hinder to practice of farming product secured credit fully in Ethiopia. Firstly, it is difficult to perfect the interests of lenders in farming product collaterals since farming products are not suitable to be described in a manner that reasonably allows their identification in the collateral registry. This will discourage lenders to receive the farming product as collateral. Secondly, it does not protect buyers of farming products in the ordinary course of the seller's business from competition from secured creditors since the proclamation gives an exclusive priority right to the latter. This destructs the marketability of farming products and thereby discourages debtors to use their farming products as collateral. Thirdly, as farming products are exposed to risks or natural catastrophes and, most farmers cannot afford to buy an insurance policy for collateralized properties, lenders may not be interested to enter into a secured transaction using a farming product.*

**Keywords:** - Collateral, Farming Products, Practicability, Secured Creditor, Security interest,

## Introduction

Intending to facilitate the transaction, many nations in the world reformed their secured transaction law.<sup>1</sup> Widening of the lists of properties that debtors can grant as collateral takes the

---

\* LL.B (Dire Dawa University), LL.M in Business and Corporate Law (Bahir Dar University), Lecturer, School of Law, Bahir Dar University. The author thanks the anonymous reviewers for their critical comments on the draft manuscript. The author can be reached at tajebe01@gmail.com

<sup>1</sup> European countries especially central and eastern countries and African countries such as Malawi, Nigeria, Sierra Leon, and Liberia are among the countries that have reformed their secured transaction law lately. (Asress Adimi Gikay, 'Rethinking Ethiopian Secured Transactions Law through Comparative Perspective: Lessons from the Uniform Commercial Code of the US', 1 Mizan Law Review 11, 154 (2017).

primacy, among others, that reforms brought in many jurisdictions.<sup>2</sup> Likewise, the Ethiopian government reformed the country's movable property security right law in August 2019 aiming to ease getting finance in the country.<sup>3</sup> Before the reform, secured transaction rules of the country were scattered in different proclamations including the Civil Code and Commercial Code.<sup>4</sup> Now, the legislature proclaims a comprehensive Movable Property Security Rights Proclamation that applies to security rights created in movable property. This Proclamation comes up with an extensive list of movable properties over which a security right can be created.<sup>5</sup> Among these lists, the farming product is one. The proclamation explicitly lists farming products as movable property that a debtor can use as collateral to secure his debt. According to this proclamation, a farmer can grant as collateral farming products including but not limited to;

*[C]rops grown, growing or to be grown, forest, timber, and other wood products, livestock, born or unborn, bees and poultry, and the produce and progeny thereof, supplies used in the farming operation, or products of livestock in their unmanufactured states are some of the farming products listed as a movable property subject to security right.<sup>6</sup>*

Allowing farmers to use farming products as collateral is a crucial means of boosting the accessibility of finance for farmers in the country. It becomes very important given that the majority of the population in Ethiopia engages in the agricultural sector.<sup>7</sup> It is, however, questionable whether secured credit backed by farming products would be pragmatic. Particularly, it is doubtful whether the interest of the lender would be secured when the collateral is a farming product. This concern becomes worrisome when we think of the difficulties in describing farming products during the perfection of the security interest, the impact of the absolute priority right of a secured creditor in the farming product collateral on the marketability of the farming products, and the catastrophes associated with farming products. Hence, this

---

<sup>2</sup>Xuan-Thao Nguyen & Bich T. Nguyen, 'Transplanting Secured Transactions Law: Trapped in the Civil Code for Emerging Economy Countries', 1 North Carolina Journal Of International Law And Commercial Regulation 40, 11 (2014).

<sup>3</sup> Movable property security rights proclamation, (2019), Fed. Neg. Gaz., Proc. No. 1147, 25<sup>th</sup> year, No. 76.

<sup>4</sup>Commercial Code of the Empire of Ethiopia, (1966), *Negarit Gazzeta* (Extraordinary issue), Proc. No. 166, 19<sup>th</sup> year, No. 3, art 947-958 & 171-193, and Civil Code of the Empire of Ethiopia, 1960, *Neg. Gaz.* ( Extraordinary issue), Proc. No. 165, 19<sup>th</sup> year, No. 2, art 2825-2874 & 3041-3130.

<sup>5</sup> Movable property Security Rights Proclamation, supra note 3, art 2/27.

<sup>6</sup>*Ibid.* Art. 2/16.

<sup>7</sup>Obse M. Eshetu, *Determinants of credit constraints in Ethiopia*, Master's Thesis in Economics, Norges Arktiste University, (2015), at. 1

paper aims at examining the practicability of farming product secured credit in light of these concerns.

The paper has two major parts. The first part deals with the general conceptual understanding of secured transactions. In this part, the author attempts to elaborate the definition of a secured transaction as well as the five stages of secured transaction namely the creation, attachment, perfection of security interest, priority among creditors, and enforcement of security rights. This helps to give some insight on the concept of secured transactions in general and to have a benchmark to evaluate the feasibility of farming product secured credit in Ethiopia. The second part analyzes the practicability of farming product secured credit in Ethiopia by considering some critical issues involved therein.

## 1. The Conceptual Underpinning of Secured Transaction

Normally, when a lender gives a loan to a borrower, it is with the expectation that the latter will pay it back. However, this may not be always the case as the borrower may sometimes default. To avoid the risks of defaults of the borrower, many lenders prefer to give a loan through a secured transaction/credit system. The term secured transaction lacks a single accepted definition.<sup>8</sup> Literally, a transaction is considered as a secured transaction when “a property is provided by the borrower (the debtor) under the terms of a loan to the lender (the secured creditor) to secure future repayments, with the lender being able to foreclose on the collateral if the borrower defaults on payment.”<sup>9</sup> From this, it can be inferred that a secured credit enables the creditor to have a claim over specific property of the debtor or third party granted as collateral provided the debtor defaults. When the transaction is secured, a security interest is created in the asset of the debtor in favor of the creditor until the settlement of the debt.<sup>10</sup> The secured transaction enables the lender to acquire a priority right in the collateralized asset of the debtor.<sup>11</sup> It helps the lender to have a right that overrides other competing creditors’ rights<sup>12</sup> and entitles

---

<sup>8</sup>Iyare Otabor-Olubor, *A Critical Appraisal of Secured Transactions over Personal Property in Nigeria: Legal Problems and a Proposal for Reform*, Ph.D. dissertation, Nottingham Trent University, (2017), P. 3

<sup>9</sup>*Ibid.*

<sup>10</sup>Otabor-Olubor, *Supra* note 8, at 3.

<sup>11</sup> Thomas H. Jackson & Anthony T. Kronman, ‘Secured Financing and Priority among Creditors’, 6 *Yale Law Journal* 88, 1143 (1979).

<sup>12</sup> *Ibid.* 1144.

him to foreclose, sell without judicial help, the collateral to satisfy his interest. Besides, it also unravels a chance for borrowers to get funds easily by securing the lender's interest.<sup>13</sup>

## 2. The Agricultural Sector and Access to Credit in Ethiopia

As different pieces of literature reiterated, the agricultural sector is the backbone of the Ethiopian economy. It contributes 46.7% to the country's Gross Domestic Product (GDP), employs 85 % of the labor force and 90% of the export products come from this sector.<sup>14</sup> Because of these contributions of the sector, Ethiopia needs to work to flourish the agricultural sector. One of the determinants for the development of the agricultural sector is the availability of finance. In practice, however, the agricultural sector has been faced inaccessibility of credit from financial institutions due to lack of physical asset collateral and other risks.<sup>15</sup> Most lenders have preferred to accept immovable property collaterals such as buildings and houses located in the urban areas or some special movables property collaterals such as vehicles.<sup>16</sup> Their inclination to lend through farming product collateral is very low. Though the law did not prohibit accepting farming products, for practical reason, lender hesitates to lend by receiving animals, forestry, and other agricultural products. As a result, farmers have not been able to get funds from lenders since they do not have immovable and special movable properties. Even farmers were not able to grant their land as collateral for their obligation since they lack ownership right on the land.<sup>17</sup>

Importantly, the present proclamation explicitly rectifies such challenges of farmers, at least theoretically, due to two reasons. On the one hand, this Proclamation explicitly allows farmers or other persons to use farming products as collateral to secure their obligation. They can get credit

---

<sup>13</sup>Ronald J. Mann, 'Explaining the Pattern of Secured Credit', 3 Harvard Law Review 110, 638-639 (1997).

<sup>14</sup>Doreen Auma and Philip Ahen Mensah, *Determinants of Credit Access and Demand Among Small-Holder Farmers in Tigray Region, Ethiopia*, Norwegian University of Life Sciences School of Economics and Business, Master's Thesis, (2014), p. 10

<sup>15</sup>Atkilt Admasu and Issac Paul, Assessment on the Mechanisms and Challenges of Small Scale Agricultural Credit from Commercial Banks in Ethiopia: The Case of Ada'a Liben Woreda Ethiopia, *Journal of Sustainable Development in Africa*, (2010), Vol.12, No.3, P. 305

<sup>16</sup>New Business Ethiopia, 'Ethiopia's smallholder farmers to use cattle as collateral', <https://newbusinessethiopia.com/finance/ethiopias-smallholder-farmers-to-use-cattle-as-collateral/> last accessed on December 11, 2019

<sup>17</sup>International Maize and Wheat Improvement Center, *Financial Products For Farmers And Service Providers Report Ethiopia*, (2015), p. 11

by granting their farming products including “crops<sup>18</sup> grown, growing or to be grown, forest, timber, and other wood products, livestock, born or unborn, bees and poultry, and the produce and progeny thereof, supplies used in the farming operation, or products of livestock in their unmanufactured states” as collateral.<sup>19</sup> On the other hand, this Proclamation imposes a mandatory obligation on commercial banks and microfinance institutions to accept farming products collaterals. The National Bank of Ethiopia (NBE) in its directive on the Operationalization of Collateral Registry mandatorily requires banks to allocate at least 5% of their credit disbursement of the year to persons engaged in the agricultural sector by receiving movable property as collaterals, which includes farming products.<sup>20</sup> These reforms in the new movable property security rights law will unravel financial access to farmers since it allows them to grant their farming products as collateral.

### 3. The Major Steps and Features of Secured Transaction under the New Proclamation

Commonly, a secured transaction process has five stages.<sup>21</sup> These are (1) creation of a security interest, (2) attachment of the interest, (3) perfection of the interest, (4) priority from other competitor creditors, and (5) enforcement of the security right by the creditor.<sup>22</sup> In fact, not every secured transaction goes through all these steps. In most cases, the secured transaction passes only the first three consecutive stages since they are essential steps to secure and perfect the interests of the creditor in collateral. The last two stages exist only when there are more than one competing creditors and there is a default of the debtor to perform his obligation respectively. A further discussion is given below about each stage of a secured transaction in reference to the new Proclamation.

---

<sup>18</sup>Crop means a plant planted cultivated for either profit-making or personal consumption. Crops can be categorized into six groups: “food crops, for human consumption (e.g., wheat potatoes); feed crops, for livestock consumption (e.g., oats, alfalfa); fiber crops, for cordage and textiles (e.g., cotton, hemp); oil crops, for consumption or industrial uses (e.g., cottonseed, corn); ornamental crops, for landscape gardening (e.g., dogwood, azalea); and industrial and secondary crops, for various personal and industrial uses (e.g., rubber, tobacco)” (<<https://www.britannica.com/topic/crop-agriculture>>last accessed on 11 December 2019).

<sup>19</sup>Movable property Security Rights Proclamation, supra note 3, Art. 2/16.

<sup>20</sup>National Bank of Ethiopia, Operationalization of Collateral Registry, Directive No. MCR/01/2020, Art. 19.1.

<sup>21</sup>Ali Khan, ‘Secured Transaction Final review 2012’, (3 December 2012) <<https://www.youtube.com/watch?v=-Tk-eO13blk&t=320s>> last accessed on 12 December 2019.

<sup>22</sup>Ibid.

### 1.1. Creation of Security Interest

The term security interest is used interchangeably with security rights in different pieces of literature. The author of this paper also uses them interchangeably. The term security right is defined by the United Nations Commission on International Trade Law (UNCITRAL) as “a property right in a personal property, created by agreement which secures payment or performance of an obligation, regardless of whether the transacting parties had delineated it as a security right.”<sup>23</sup> The Ethiopian secured transaction law also provides a similar definition. It is defined as “a property right in a movable property that is created by an agreement to secure payment or other performance of an obligation, regardless of whether parties have denominated it as a security right, the status of the grantor or secured creditor, or the nature of the secured the obligation”.<sup>24</sup> From these two definitions, it can be understood that a security right is a right created in movable property in favor of a creditor through the conclusion of a valid security agreement between a creditor and a debtor. Here, a security agreement means a contractual agreement that the debtor agrees with a creditor to grant his property as a security to secure the re-payment of the loan that he took or the performance of his obligation.<sup>25</sup>

Security agreements, like other types of contractual agreements, shall fulfill the validity requirements provided by the general contract law.<sup>26</sup> However, there are special validity requirements for a security agreement provided by the Ethiopian movable security rights proclamation. The proclamation provides four special validity requirements for the validity of a security agreement. First, the agreement shall be made in writing; and the grantor shall sign it.<sup>27</sup> Security agreement cannot be made orally. Making security agreements in writing is important for evidentiary purposes. The grantor of the collateral must also sign the agreement. Nevertheless, the signature of a secured creditor is irrelevant to the validity of the agreement. Second, the agreement shall contain the description of the secured obligation.<sup>28</sup> The agreement should specify clearly the obligation of the debtor secured by the collateral. As it is provided in

---

<sup>23</sup>Otabor-Olubor, *supra* note 8, at 3.

<sup>24</sup>Movable property Security Rights Proclamation, *supra* note 3, Art. 2/44.

<sup>25</sup>Marek Dubovec & Cyprian Kambili, *A Guide to the Personal Property Security Act: The Case of Malawi*, Pretoria University Law Press, 52 (2015).

<sup>26</sup>Civil Code of the Empire of Ethiopia, *supra* note 4, Art. 1678 ff.

<sup>27</sup>Movable property Security Rights Proclamation, *supra* note 3, Art. 4/5.

<sup>28</sup>*Ibid.* Art. 4/5 (b).

the proclamation, the obligation that can be secured by collateral is an unlimited one. It could be one or more than one of any type, present or future, determinable or determined, conditional or unconditional, fixed or fluctuating.<sup>29</sup> The obligation of the debtor may be to return the loan that he took, or it may be the performance of any other obligation. In any case, such obligation should be described in the security agreement in a way that it can be reasonably identified.<sup>30</sup>

Third, the agreement shall include a clear description of the collateral granted to secure the interests of the creditor.<sup>31</sup> As mentioned above, a debtor is expected to grant a property as collateral to secure the rights of the creditor. The property that is given as collateral shall be described succinctly. The difficulty is, then, what kind of description is said to be ‘reasonable’ to identify the collateral. This issue may vary depending on the nature of the property to be granted as collateral. Therefore, whatever the nature of the collateral is, the law requires it to be identified in the agreement by using their specific listings, category, type of collateral, or quantity.<sup>32</sup>

A closer reading of the proclamation shows that collaterals could be corporeal and incorporeal. Corporeal includes any tangible goods including money, negotiable instruments (promissory note, bills of exchange, and others other than a cheque<sup>33</sup>), negotiable documents (bills of lading, warehouse receipt, seaway bill, and other), and certificated securities (share/stock, bond, debenture, and treasury bills).<sup>34</sup> An incorporeal asset, on the other hand, includes properties other than those falls under the category of corporeal assets including receivables<sup>35</sup>, deposit account<sup>36</sup>, and intellectual property rights.<sup>37</sup> These properties may be existing or to be acquired

---

<sup>29</sup>*Ibid.* Art. 5.

<sup>30</sup>*Ibid.* Art. 6/1.

<sup>31</sup>*Ibid.* Art. 4/5 (c).

<sup>32</sup>*Ibid.* Art. 6/1.

<sup>33</sup>The nature of a cheque is payable on demand or at sight i.e. the holder can claim payment from the drawee as soon as he receives the instrument without waiting any further periods. Because of this nature, a cheque cannot be used as a pledge or security to secure the interests of secured creditors. (ገዙ አየለ መንግስቱ, የኢትዮጵያ የባንክ እና የሚተላለፉ የንግድ ሰነዶች ሕግ, 162 (2009)).

<sup>34</sup>Movable property Security Rights Proclamation, *supra* note 3, Art. 10.

<sup>35</sup>Receivable refers to “a right to payment of monetary obligation, excluding a right to payment evidenced by a negotiable instrument, a right to payment of funds credited to a deposited account and a right to payment under security.” (*Ibid.* Art. 2/37).

<sup>36</sup>A deposit account refers to "an account maintained by a financial institution authorized to receive a deposit from the public" (*Ibid.* Art. 2/13).

<sup>37</sup>*Ibid.* Art. 2/22.

in the future. For example, a debtor may grant his existing vehicle or his vehicle that he plans to buy after two months.

Fourth, the agreement shall also include the description of parties involved in the contractual agreement in a way that a secured creditor and the grantor can be easily identified. The agreement shall identify who is the grantor, the debtor, and who is the creditor.<sup>38</sup> Overall, upon the conclusion of a valid security agreement, there is a creation of security interest in favor of the creditor and, then, the first stage of the secured transaction is done.

### 1.2. Attachment of Security Interest

The mere conclusion of a secured transaction may not give a creditor a security right in the collateral property.<sup>39</sup> The creditor's right remains to be contractual unless his interest is attached.<sup>40</sup> Before attachment, the secured creditor's claim is limited to the breach of the contractual agreement and does not have any claim in specific collateral or asset of the debtor.<sup>41</sup> The creditor acquires enforceable interest to be claimed against the collateral only if there is an attachment of the interest.<sup>42</sup> A security interest is considered as attached provided, first, there is a conclusion of a valid security agreement.<sup>43</sup> As mentioned before, the conclusion of a security agreement is the basis for any secured transaction.<sup>44</sup> Therefore, there shall be a valid security agreement to attach a security interest. Second, the debtor is an owner of the collateral or has a right to encumber it.<sup>45</sup> This is because the creditor will not be able to exercise his right through foreclosure or re-possession unless the debtor is an owner or has a right to transfer to third parties. Third, the debtor received some value (loan) from the creditor.<sup>46</sup> There is no security interest unless the debtor receives some gain or benefit from the creditor i.e. the security right is not enforceable until the creditor gave the debtor some value, be it a loan or else.

---

<sup>38</sup>*Ibid.* Art. 4/5 (a).

<sup>39</sup>Dubovec & Kambili, *supra* note 25, at 53.

<sup>40</sup>*Ibid.*

<sup>41</sup>*Ibid.*

<sup>42</sup>*Ibid.*

<sup>43</sup>Movable property Security Rights Proclamation, *supra* note 3, Art. 4/1.

<sup>44</sup>*Supra*, p. 6, Section 1.1, Para. 1.

<sup>45</sup>Movable property Security Rights Proclamation, *supra* note 3, Art. 4/1.

<sup>46</sup>*Ibid.* Art. 4/1.



Thus, if all of these requirements of attachment are fulfilled, the security interest becomes enforceable. The creditor acquires an enforceable security right in collateral that can be exercised upon the default of the debtor.

### 1.3. The Perfection of Security Interest

The creation and attachment of security interest may not necessarily mean that the secured creditor is certain to enforce his right in the collateral upon the debtor's default. Rather, the secured creditor needs to proceed with further steps to perfect his right. Perfection of a security interest is the “process of putting the entire world on notice that the secured party claims a security interest in the debtor’s collateral”.<sup>47</sup> It is a means of making the security interest enforceable against third parties who have a competing claim in the same collateral.<sup>48</sup> The perfection of security interest protects the interests of secured creditors by excluding third parties, such as buyers and other creditors, from having a claim in the collateral. A secured creditor, to perfect his right, is required to put the world in a notice by different methods so that other potential creditors refrain from receiving such collaterals as security.<sup>49</sup> The methods of perfecting security interests vary depending on the nature of the property granted as collateral. In any case, there are four major methods of perfection of security interest recognized in different jurisdictions.<sup>50</sup> These are perfection through registration, possession, control, and automatic methods.<sup>51</sup> All of these methods of perfection are also incorporated under the Ethiopian Movable Property Security Rights Proclamation.

#### 1.3.1. Perfection by Registration

Collaterals, especially tangible assets, are preferred to be perfected through filing before the concerned authority.<sup>52</sup> Registration of security interest enables other potential creditors to verify the existence of prior established security interest in the collateral that the debtor agrees to grant as security.<sup>53</sup> Potential creditors can assure this by searching the borrower's name from the

---

<sup>47</sup>Jason Gordon, ‘Perfection of a Security Interest’, <<https://thebusinessprofessor.com/lesson/perfection-of-a-security-interest/>> accessed on April 28/2021.

<sup>48</sup>*Ibid.*

<sup>49</sup>Dubovec & Kambili, *supra* note 25, at 65.

<sup>50</sup>*Ibid.* p. 66-67.

<sup>51</sup>*Ibid.*

<sup>52</sup>*Ibid.*, at 68.

<sup>53</sup>*Ibid.*

records of the concerned authority.<sup>54</sup> The Ethiopian law also provides that the perfection of tangible assets must be through filing a notice in the collateral registry.<sup>55</sup> Of course, there is no collateral registry in Ethiopia so far. Though the proclamation requires that the collateral registry office to be established by the regulation, so far, there is no such office in the country.<sup>56</sup> However, when there is a collateral registry, it will have the purpose of receiving, storing, and making information to the society.<sup>57</sup> Perfection through registration is made by registering the name of the debtor<sup>58</sup>, secured creditor,<sup>59</sup> and collateral<sup>60</sup> using their identification such as a serial number. Thus, other creditors can access the fact by using either of such elements of registration. Even our law adopts an online filing system, which is, of course, very absurd to practice in the current reality of the country.<sup>61</sup>

### 1.3.2. Perfection by Possession

The nature of some collateral requires the perfection of the security interest in such properties to be made by possession.<sup>62</sup> Collaterals such as promissory notes, a security certificate, or a warehouse receipt into its custody should be perfected through possession.<sup>63</sup> The Ethiopian Movable Security Right Proclamation also provides that collaterals such as money, negotiable instruments, negotiable documents, and certificated securities are categories of collaterals to be perfected through possession.<sup>64</sup> The nature of these collaterals requires the creditor to possess the property itself so that he can exclude third parties from having a right in the collateral. In fact, possession may be used to perfect even security interests in tangible assets as an alternative to registration.<sup>65</sup>

---

<sup>54</sup>Steve, Weise & Stephen, L. Sepinuck, 'Personal Property Secured Transactions', 4 the Business Lawyer 68, 1268 (2013).

<sup>55</sup>Movable property Security Rights Proclamation, supra note 3, Art. 13/1.

<sup>56</sup>*Ibid.* Art. 20.

<sup>57</sup>*Ibid.* Art. 21.

<sup>58</sup>*Ibid.* Art. 28.

<sup>59</sup>*Ibid.* Art. 29.

<sup>60</sup>*Ibid.* Art. 30.

<sup>61</sup>*Ibid.* Art. 24 ff.

<sup>62</sup>Dubovec & Kambili, supra note 25, at 72.

<sup>63</sup>*Ibid.*

<sup>64</sup>Movable property Security Rights Proclamation, supra note 3, Art. 13/2. Possession could be either actual possession or constructive possession (*Ibid.* Art. 2/35).

<sup>65</sup>Dubovec & Kambili, supra note 25, at 72.

### 1.3.3. Perfection by Control

Likewise, the nature of some other properties requires to be perfected by control. If the lender controls the collateral, it means that he can exercise his right on the default of the debtor without the permission of the latter.<sup>66</sup> According to the Ethiopian Movable Property Security Rights Proclamation, payment of funds credited to a deposit account and electronic securities can be perfected through control.<sup>67</sup> Deposit accounts could be controlled through three mechanisms. First, it can be controlled through the conclusion of a tri-party control agreement.<sup>68</sup> The secured creditor controls the account by reaching an agreement with the grantor and financial institution that the financial institution should follow the orders of the creditor for any transaction. “Third-party creditors that do not maintain bank accounts could effectively control a deposit account of the debtor by requiring a bank to establish a specific collateral bank account to which all proceeds shall be deposited and the withdrawals controlled by that secured party.”<sup>69</sup> In such a case, the account is under the control of the creditor as every activity in that account is upon the creditor's instruction. Second, it can be also controlled through the creation of security interests in favor of financial institutions. If the security interest is created in favor of the financial institution, which maintains the account, that financial institution can easily control the deposit and withdrawal of money from that account.<sup>70</sup> Third, it can be also controlled when the secured creditor becomes the deposit account holder.<sup>71</sup> When the secured creditor is the account holder, he is the only person that can withdraw cash from his account. That means he is controlling his interest.

Concerning electronic securities, it can be controlled in two ways. First, it can be controlled by entering into an agreement with the grantor and issuer that the issuer must follow the instruction given by the secured creditor for whatever transaction in the electronic securities.<sup>72</sup> Second, it can be also controlled by entering or noting the secured creditor's name or his right in the book maintained for recording the name of the security holder.<sup>73</sup>

---

<sup>66</sup>Otabor-Olubor, *supra* note 8<sub>2</sub> at 160.

<sup>67</sup>Movable property Security Rights Proclamation, *supra* note 3, Art. 13/3.

<sup>68</sup>*Ibid.* Art. 17/2.

<sup>69</sup>Dubovec & Kambili, *supra* note 25<sub>2</sub> at 74.

<sup>70</sup>Movable property Security Rights Proclamation, *supra* note 3, Art. 17/1.

<sup>71</sup>*Ibid.* Art. 17/3.

<sup>72</sup>*Ibid.* Art. 19/2.

<sup>73</sup>*Ibid.* Art. 19/1.

#### 1.3.4. Automatic Perfection

Automatic perfection refers to when the interest of the creditor has perfected without any further requirements i.e. perfection of security interest by the mere fact of the creation of security interest. Rights in proceeds and acquisition security rights are prominent examples of security interests that can be perfected automatically.<sup>74</sup> As it is stated under Ethiopian Movable Property Security Right Proclamation, a security right in an asset automatically extends to its proceeds.<sup>75</sup> A secured creditor who has a security interest in an asset will automatically have a security interest in the proceeds derived from that asset without additional perfection requirements. A proceed, here, refers to “whatever received from the collateral including from selling, licensing, insurance, fruits, claims arising from defects, damage or loss of the collateral and also proceeds of proceed.”<sup>76</sup>

Similarly, if the interest of a person is secured by acquisition security right, his security interest will be perfected automatically. A right is said to be an acquisition right when “a security right in a corporeal asset or intellectual property, which secures the obligation to pay any unpaid portion of the purchase price of the asset or other credit extended to enable the grantor to acquire right in the asset to the extent the credit is used for that purpose.”<sup>77</sup> This means when the creditor and borrower conclude a purchase-money agreement i.e. the loan is said to be a purchase price for the asset that the borrower plans to buy, an acquisition security right is created in favor of the lender. Through automatic perfection, the lender of money in the form of a purchase-price agreement will acquire a super-priority right even against interests perfected before such an agreement.<sup>78</sup> In fact, to acquire this right, a creditor needs to meet some procedures provided by the proclamation.<sup>79</sup>

#### 1.4. Priority among Creditors of Security Right

It is obvious that a secured creditor has a priority right in the collateral against unsecured creditors of the same debtor.<sup>80</sup> In some cases, however, a difficulty may arise to establish the

---

<sup>74</sup>Dubovec & Kambili, *supra* note 25, at 66 & 78

<sup>75</sup>Movable property Security Rights Proclamation, *supra* note 3, Art. 7/1.

<sup>76</sup>*Ibid.* Art. 2/36

<sup>77</sup>*Ibid.* Art. 2/2.

<sup>78</sup>*Ibid.* Art.56.

<sup>79</sup>To know detail procedural requirements to get super-priority interest over acquisition security rights see Movable property Security Rights Proclamation, *supra* note 3, Art. 56.

<sup>80</sup>Jacksonm & Kronman, *supra* note 11, at 1161.

order of creditors’ interest when two or more creditors have a claim in the same asset of the same debtor.<sup>81</sup> This problem becomes worse when the debtor’s asset is insufficient to pay the claims of all creditors. To address such a problem, most secured transaction legislations set priority rules to determine the rank of creditors.<sup>82</sup> Once a secured creditor gets priority right in the collateral, he can be paid fully before other subordinate creditors.<sup>83</sup>

The Ethiopian Movable Security Rights Proclamation also came up with detailed rules of priority among competing creditors of a debtor in the same collateral. Of course, the priority rules incorporated in the proclamation may differ depending on the type of the collateral and the aligned methods of perfecting the security right. In principle, when collateral is a tangible asset the ranks of the creditors are determined based on the time of registration in a collateral registry office.<sup>84</sup> The competition in the same corporeal asset needs to be settled based on the maxim “[t]he first in time, the first in right”. (Emphasis added).<sup>85</sup> The proclamation, however, provides special means of determination of the rank of creditors when the collateral is intangible property. As regards deposit account and electronic securities, the one who is the holder of such property will have an overriding right.<sup>86</sup> Should the property is money, negotiable instruments, negotiable documents, or certificated securities, the person who has possession of such properties will be the winner in the competition of creditors. To know the detailed rules in the proclamation in respect to establishing the ranks for competing creditors, see the summary given below.

Table 1. Summary of the Priority Rules of the Ethiopian Movable Property Security Rights Proclamation

Competing Creditors	Collateral Type	Overriding Creditor
Secured creditor Vs. Unsecured creditor	Any collateral type	Secured creditor (art. 45/1).
A creditor with perfected security interest Vs. A creditor with unperfected security	„	A creditor with perfected security interest (art. 13).

<sup>81</sup>*Ibid.* at 1162

<sup>82</sup>Dubovec & Kambili, *supra* note 25, at 83

<sup>83</sup>Douglas G. Baird, ‘Priority Matters: Absolute Priority, Relative Priority and the Costs Of Bankruptcy’, 165 *University Of Pennsylvania Law Review* 4, 785 (2017), at. 786

<sup>84</sup>Movable property Security Rights Proclamation, *supra* note 3, Art.13/1 & art. 46/1.

<sup>85</sup>Jacksonm & Kronman, *supra* note 11, at 1161.

<sup>86</sup> Movable property Security Rights Proclamation, *supra* note 3, Art. 62/1 & 65/2.

interest		
A creditor with perfected security interest Vs. A creditor with perfected security interest	„	A creditor that registers the interest first, possesses or controls the collateral depending on the type of the collateral (art. 13 & 46).
Secured creditor Vs. Buyer, licensee, or lease of the collateral	„	Secured creditor unless the secured creditor authorizes the sale or transfer of the asset free of security right or the transaction is made in the ordinary business course of the seller and the transferee doesn't know that the transfer violates creditor's right (art.54).
A creditor whose interest is secured by collateral before commingling with other good Vs. A Creditor whose interest is secured by collateral after commingling with other good	Tangible properties	A creditor whose interest is secured with collateral before commingling with other good (art. 52/1).
A creditor whose interest is secured by collateral before commingling with other good Vs. A creditor whose interest is secured by collateral before commingling with other good	„	All creditors are entitled to proportionate to the value of their respective collaterals before commingling (art. 52/2).
A creditor whose interest is secured by acquisition security right Vs. A creditor whose interest is secured by non-acquisition security right	IP rights Equipment Consumer goods	Acquisition creditor provided he is in possession of the collateral (art. 56/1(a)) or registered within seven days from the date of acquisition (56/1(b)).
	Inventory	A creditor in possession of the collateral (art.56/2(a), or registered the interest before the grantor obtains possession of the property and gives notice of the existence of acquisition right for the no-acquisition creditor (56/2 (b & c)).
A creditor whose interest is secured by acquisition right Vs. A creditor whose interest is secured by acquisition right	All types of collateral	An acquisition creditor who is first in registering the interest, possesses or controls the collateral unless the acquisition right holder is the seller, lessor or licensor (art. 57).

Secured creditor Vs. Transferee	Negotiable instrument	Transferee provided he is a holder in due course and took the possession with value without the knowledge that the sale violates the creditor's right (art. 61/2).
A creditor whose security right is secured by registration Vs. A creditor whose security right is secured by possession	Negotiable instruments	A creditor whose security right is secured by possession (art. 61/1).
A creditor with unperfected security interest Vs. A creditor with unperfected security interest	Any type of property	The proclamation is silent. Hence, it is open for argument whether the rights of competing creditors' rights should be ranked based on the date of registration of the interest, or proportionately to their right.
A creditor whose security right is perfected through becoming an account holder Vs. A creditor whose security right is perfected through other methods	Deposit account	A creditor whose security right is perfected through becoming an account holder (art. 62/1).
Financial institution creditor with perfected security right Vs. Non-financial institution creditor with perfected right	Deposit account	Financial institution creditor with perfected security right unless the non-financial creditor is an account holder (art. 62/2).
A creditor whose security right is perfected by control agreement Vs. A creditor whose right is perfected by other methods	Deposit account	A creditor whose security right is perfected by a control agreement the creditor is a financial institution or an account holder (art. 62/3).
A creditor whose security right is perfected by concluding control agreement Vs. A creditor whose right is perfected by concluding control agreement	Deposit account	The first in concluding the control agreement prevails (art. 62/4).
Financial institution's set off right Vs. Secured creditor right	Deposit account	Financial institution's set off right unless the secured creditor is the account holder (art. 62/5).
Transferee Vs. Secured creditor	Deposit account	Transferee unless he knows the transfer violates the rights of the secured creditor (art. 62/6).
Transferee Vs. Secured creditor	Money	Transferee unless he knows the transfer violates the rights of the secured party (art. 63).
A creditor whose security right is perfected by possession of negotiable document Vs. A creditor whose right is secured by other methods	Negotiable document	A creditor whose right is perfected by possession of the negotiable document (art. 64/1).
A Transferee who possesses the document Vs. A secured creditors	Negotiable document	Transferee unless he knows the transfer violates the rights of the

		secured party (art. 64/2).
A creditor whose interest is perfected by possession Vs. A creditor whose interest is perfected by registration	Certificated Securities	A creditor whose interest is perfected by possession prevails (art. 65/1).
A creditor whose security interest is perfected by notation/registration the name of the secured creditor in the record book Vs. A creditor whose interest is secured by other methods	Electronic security	A creditor whose interest is perfected by notation/registration the name of the secured creditor in the record book prevails (art. 65/2).
A creditor whose security interest is perfected by the conclusion of control agreement Vs. A creditor whose interest is secured by registration	Electronic security	A creditor whose interest is perfected by a control agreement (art. 65/3).
A creditor whose security interest is perfected by concluding control agreement Vs. A creditor whose security interest is perfected by concluding control agreement	Electronic security	The first in concluding the control agreement prevails (art. 65/4).
A transferee who possesses the security Vs. secured creditors	Electronic security and Certificated Securities	Transferee unless he knows the transfer violates the rights of the secured party (art. 65/5).

### 1.5. Enforcement of Security Rights

Though the debtor has a contractual obligation to pay back the loan, he may fail to do so due to different reasons and, then, it can be said that there is a default of the debtor. If there is a default, the secured creditor has an option to receive his money through “recours[ing] to the collateral of the debtor.”<sup>87</sup> Under the Ethiopian Movable Property Security Rights Proclamation, a secured creditor has three major alternatives of enforcement provided there is a default of the debtor. These are enforcement through the foreclosure system<sup>88</sup>, repossession<sup>89</sup> and judicial help<sup>90</sup>. Though the proclamation does not use the term ‘foreclosure’ exactly, it entitles the secured creditor to sell or otherwise dispose of the collateral without demanding the judgment of a court.<sup>91</sup> The secured creditor, however, needs to give a ten days’ notice to the grantor or any other person who possesses or has a right in the property.<sup>92</sup> He shall notify the debtor of his

<sup>87</sup>Dubovec & Kambili, *supra* note 25<sub>2</sub>, at 83.

<sup>88</sup>Movable property Security Rights Proclamation, *supra* note 3, Art. 82 & 83.

<sup>89</sup>*Ibid.* Art. 81.

<sup>90</sup>*Ibid.* Art. 77.

<sup>91</sup>*Ibid.* Art. 82.

<sup>92</sup>*Ibid.* Art. 83/1.



intention of disposition. By doing so, the secured creditor may sell the property through public auction following the rule of public auction under the civil procedure code of Ethiopia.<sup>93</sup> Enforcing the right through foreclosure helps to avoid the prolonged court process.<sup>94</sup>

Execution of security rights through self-help/repossession means taking possession of the thing and using it for personal purposes without court proceedings. As it is given under the proclamation, the secured creditor can enforce his right through possession provided there is either (1) agreement to repossess in the security agreement<sup>95</sup> or (2) the grantor or any other person who possesses the property does not object in the attempt of repossession by the secured creditor.<sup>96</sup> The other alternative to the enforcement of security rights is through court proceedings. This is claiming payment from the defaulting debtor through a judicial process. A secured creditor can claim his right by instituting court action against the debtor. This alternative is, in fact, tiresome and costly since it takes an extended period. Consequently, it is not recommended unless the other alternatives are absent or failed to solve the dispute.

## 2. Problems for Using Farm Products as a Collateral under the Proclamation

### 2.1. Description of Farming Product in Perfecting Security Interest

As discussed in the first part of this paper, a secured creditor needs to perfect his security interest to have perfect security rights.<sup>97</sup> Otherwise, his security right will be subordinate to the security right of another third-party creditor who has a security interest in the same collateral and debtor. As well, a creditor whose security interest is secured by farming products shall perfect his interest. As farming products are tangible properties, the lender has two alternative methods of perfection. It can be done either through possession of the collateral or registration of the interest in the collateral registry. However, perfecting security interest in farming products through possession, in most cases, is problematic. This is because, on the one hand, if the lender possesses the collateralized farming product, it will result in the dispossession of the borrower. Dispossession, in turn, inhibits him from using the collateral, which may discourage borrowers to

---

<sup>93</sup>*Ibid.* Art. 82 (3 &4).

<sup>94</sup>Tihitina Ayalew, *Legal Problems in Realizing Non-Performing Loans of Banks in Ethiopia*, Addis Ababa University school of law, LLM thesis, (2009), at 54

<sup>95</sup>Movable property Security Rights Proclamation, supra note 3, Art. 81/1(a).

<sup>96</sup>*Ibid.* Art. 81 1 (b).

<sup>97</sup>Supra, p. 9, Section 1.3, Para. 1.

use their farming products as collateral. Of course, farming products kept in a warehouse can be perfected through possessing the warehouse receipt without which the borrower cannot sell such warehoused goods. In such a case, it is straightforward to perfect interests in farming products stored in a warehouse. On the other hand, the nature of some farming products does not permit perfection through possession. It is impossible, for example, to possess crops growing or to be grown and unborn livestock. Especially, it is ridiculous for a financial institution to take possession of farming products. It is unthinkable, for example, for a bank to possess a camel or cow until the settlement of the debt. Hence, except for products stored in a warehouse, the interest of a creditor is better to be perfected through registration.

Yet, perfecting the a security interest in farming products through registration is not flawless. As it is specified under the proclamation, during the registration of security interest in the collateral registry, the collateral shall be described in “*a manner that reasonably allows their identification*” (*emphasis added*).<sup>98</sup> This requirement is set to inform other creditors about the preexisting security interest easily through online searching. Besides, the NBE directive on Codification, Valuation, and Registration of Movable Properties as Collateral for Credit indicates some manners of describing the farming products in a collateral registry. Concerning livestock collateral, it requires that the registration to describe the livestock using the ear tag number of the livestock, which is codified and supplied by the ministry of agriculture or its authorized distributors.<sup>99</sup> Nevertheless, this method of description is not sufficient to allow the identification of the collateral by other potential lenders. First, it is very challenging to supply a plastic ear tag number for livestock in remote areas. It is also hardly possible to describe future animal collaterals using ear tag number. It is very tricky to describe reasonably, for example, the unborn animal in perfecting the interest in the collateral. It is also too difficult to describe reasonably the bee and poultry collateral.

Second, though the directive requires any livestock collateral to be codified by the plastic ear tag number, it is uncertain that the ear tag number will keep on the ear of the livestock until the settlement of the credit. It may be damaged, cut-off or the owner of the livestock may intentionally detach the plastic ear tag after he receives the loan. This could deny potential

---

<sup>98</sup>Movable property Security Rights Proclamation, supra note 3, Art. 30/1.

<sup>99</sup> National Bank of Ethiopia, Codification, Valuation, and Registration of Movable Properties as Collateral for Credit, Directive No. 186/2020, art. 5.3

lenders to verify the existence of security interest on the livestock. In fact, the directive tries to minimize such problems by requiring the grantor to report whenever the ear tag is damaged, lost or detached which, otherwise, results in the early settlement of the credit or possession of the livestock by the secured creditor.<sup>100</sup> However, this works only when there is close supervision of the collateral by the secured creditor. In the Ethiopian case, it is difficult that lenders would make close supervision of the livestock collateral in remote areas. Therefore, it is very challenging to inform other potential creditors by describing livestock in the collateral registry using the plastic ear tag number.

For the same reason, it is very hard to describe crops in a way that reasonably allows their identification. Like the case of livestock, the directive on codification, valuation, and registration of movable properties as collateral for credit provides the manner of describing the crop. Crop collateral is required to be described using the tax identification number of the owner, the unique parcel identification number of the landholding certificate of the person who offered it as collateral for the credit; the type of crop being pledged, the expected maximum output and the maximum output to be pledged for credit.<sup>101</sup> Looking the practice in other jurisdictions, for example, in the USA, “indicating the name of the owner of the land, approximate number of acres, the [state] the land is in, popular name, [and] the appropriate distance from a named town or well-known landmark” is sufficient to notify other creditors who will look for such information.<sup>102</sup> However, in Ethiopia, it is very tough for those lenders who reside in town to go to remote rural areas and try to get such information regarding the crop since the country lacks an infrastructure to do so. It is very challenging that a bank, for example, to send its loan officers too far distance in the rural areas (with poor infrastructure) to observe whether the said crop exists, to identify the type of crop harvested, assess the maximum amount from the collateralized crop, its distances from the town, to measure the land’s acre and other related specifications. Thus, description of crop collateral is not easy if the crop is being harvested in remote areas.

Of course, the description can be made using wide-ranging expressions such as ‘all existing and future animals’ or ‘all existing and future crops’. Such description in the collateral registry will

---

<sup>100</sup> *Ibid.* art. 5.6.4

<sup>101</sup> *Ibid.* art. 6.3

<sup>102</sup> Keith G. Meyer, ‘The 9-307(1) Farm Products Puzzle: Its Parts and Its Future’, *North Dakota Law Review* 60, 417 (1984).

adequately inform other prospective creditors of the debtor at least by looking the name of the debtor in the registry. From the perspective of the secured creditor, it is the best advisable means of describing farming products in general terms. Because the security interest is extended to all the existing and future animals or all the existing and future crops, the secured creditor will have an overriding interest in such general assets of the borrower in case he defaults. Nevertheless, such kind of transaction affects the interests of farmers adversely. Once a farmer grants all his animals or crops to secure his loan, he will not have any property left to be used as collateral if he needs an additional loan. The farmer will benefit should the collateral is a specific farming product saving the challenges in the description. Thus, it is very challenging to use specific farming products, other than warehoused goods, as a security to get a loan from lenders. The farmer can get a loan only if he grants all his crop products and/or animals as security and the location of such properties is near to a town. Except this, farming products secured credit will not be fully pragmatic as much as the new movable property security right proclamation intends.

## 2.2. Competition between Secured Creditors and Potential Buyers

It is obvious that a farmer to trade with his farming products to generate an income for different purposes. He may sell, for example, a farming product granted as collateral for the loan he has borrowed from the lender for celebrating his child's wedding. In such a case, an important concern may arise. That is, what would be the fate of the secured creditor whose interest is perfected before the sale? Alternatively, should a buyer take that farming product free from any security interest or prior claim?

Regarding this issue, there are two lines of scholarly proposed arguments. Some scholars argue that buyers of a collaterally given farming product shall be allowed to take it free from any claims of secured creditors.<sup>103</sup> To substantiate their argument, they put forward the following reasons. First, they argue that unless buyers of farming products are allowed to take such goods free from prior interests, it will destruct the commercial expectation of good faith buyers.<sup>104</sup> Second, as the interests of the secured party extended to proceeds, the creditor can claim his interest over the proceeds of the product sold, rather than calming back from the buyer.<sup>105</sup> Third,

---

<sup>103</sup>*Ibid.* 434.

<sup>104</sup>Barkley Clar, 'Secured Transactions', 4 *the Business Lawyer* 42, 1335 (1987).

<sup>105</sup>*Ibid.*

since, in most cases, farmers need to sell their farming products to pay their debt, buyers must be allowed to take them free so that borrowers can sell their products.

In contrast, some others argue that buyers of farming products shall not be allowed to take free from secured creditor's claims. In justifying this, first, they argue that, usually, buyers of farming products are "high-level" buyers who are expected to have an experience of searching the existence of security interest over the product.<sup>106</sup> Through searching prior records, buyers can inspect the existence of secured creditors. Second, should there be permission for buyers to take such products free of encumbrance; the interests of lenders will be affected.<sup>107</sup> Hence, they must not be permitted to take free from claims of secured creditors.

In respect to this issue, the Uniform Commercial Code (UCC) of the USA passed two stages. The 1962 and 1972 text of U.C.C. provides under section 9-307(1) that "ordinary course buyers of farm products (crops or livestock) cannot take free from a prior perfected security interest covering the farm product."<sup>108</sup> In U.C.C, the phrase 'ordinary course of business is defined as a person that "buys goods in good faith, without knowledge that the sale violates the rights of another party to goods."<sup>109</sup> The main justification for this rule was to encourage lenders to lend to the agricultural sector.<sup>110</sup> However, because of the pressures of buyers of agricultural products, section 9-307 (1) of UC.C. was amended by the 1985 Federal Food Act of the USA and the amendment provides the following provision.<sup>111</sup>

*[N]otwithstanding of any other provision of federal, state or local law, a buyer who is in the ordinary course of businesses buys a farm product from a seller engaging in farming operations shall take free of a security interest created by the seller, even though the security interest is perfected; and the buyer knows of the existence of such interest.*<sup>112</sup>

---

<sup>106</sup>Meyer, supra note 97, at 434.

<sup>107</sup>*Ibid.* 435.

<sup>108</sup>Clar, supra notes 99, at 1334-1335.

<sup>109</sup>Uniform Commercial Code, section 1-201(9), (1978).

<sup>110</sup>Daniel P Johnson, 'Federal Legislation Provides Protection for Buyers of Farm Products: Food Security Act Supersedes the Farm Products Exception of UCC Section 9-307(1)', 47 U Pitt L Rev 749, 752(1986).

<sup>111</sup>Clar, supra note 99, at 1336.

<sup>112</sup>*Ibid.* 1336.

Thus, currently, according to the 1985 Federal Food Act, a buyer can take the farming product free of a perfected security interest provided he buys in the ‘ordinary course of business’ regardless of his knowledge about the existence of security interest. It shifts the risks from buyers to lenders.<sup>113</sup> Of course, this act does not neglect the interests of the lenders. The buyer takes the product subject to the security interest provided he receives written notice from the lender or seller within one year before the sale; the lender has filed its security interest in the central filing system; or the buyer failed to be registered in the central filing office before he purchases due to which the lender unable to notify its interest to potential buyers.<sup>114</sup> Generally, the current stand of the USA is that though buyers of farm products in the ordinary course of business can take free from the security interest created over the product, the buyer takes the product subject to security interest provided either of the aforementioned condition is fulfilled.

Unlike the USA, under the new movable security right law of Ethiopia, there is no an exception of ‘ordinary course of business’ when the grantor sells the collateralized farming product. The secured creditor has always an absolute priority right against any buyer of the farming product. The directive on Codification, Valuation and Registration of Movable Properties as Collateral for Credit makes the sale of a pledged farmed product without the consent of the secured creditor an offence and *requires the product sold to be transferred to the secured creditor (emphasis added)*.<sup>115</sup> This directive disregards the impact of such prohibition on the marketability of farming products. Unless buyers of farm products are allowed to take the product free of encumbrance, they may not prefer to buy such products. This is a hurdle for the commerciality of collateralized farming products. Consequently, farmers will not be able to sell their property even to get money to repay their debt. This will drain the capacity of the borrower to repay the credit he has taken from the secured creditor.

Since buyers are not permitted to take free of security interests, they are obliged to make an online search to check whether the product is covered by the preexisting security interest. This is impossible with the current reality of Ethiopia. The existing infrastructure does not allow every

---

<sup>113</sup>Keith G. Meyer, ‘A Garden Variety of UCC Issues Dealing with Agriculture’, 58 U Kan L Rev 1119, 1152(2010).

<sup>114</sup>Keith G. Meyer, ‘Current Article 9 Issues and Agricultural Credit’, 10 Drake J Agric L 105, 128 (2005) (see on the footnote).

<sup>115</sup> National Bank of Ethiopia, Codification, Valuation and Registration of Movable Properties as Collateral for Credit, Directive No. 186/2020, art. 5.6.6 and art. 6.4.4.

potential buyer to do so. There is no networks to search for and electric powers to recharge our electronic devices in every part of the country to search for it online. Therefore, it is very difficult to assume that potential buyers will be informed through public search in the collateral registry site. Even it is very challenging to give notification to the potential buyers of farming products like the case in USA, as there is no practice of registering potential buyers in a centralized registry system. Even potential buyers of such products may be illiterate ones. They may not know, for example, how the search in the collateral registry can be made. In fact, the free-taking of the collateralized farming product discourages lenders to accept agricultural products as collateral as well. If buyers are allowed to take free of encumbrance, it may result in loss of security right of secured creditor provided the borrower defaults. Yet, the lender has another opportunity i.e. to claim payment from the proceeds of the product sold as his interest extends to proceeds too.<sup>116</sup> The creditor can claim, for example, its money from the income that the borrower received because of the sale. Of course, it may be difficult to identify and claim the money collected from the sale, as it may be mingled with other bank deposits.<sup>117</sup> Even so, the law should allow, at least, buyers of the farming products in the ordinary course of business to take free of encumbrance. Otherwise, it will destruct the normal business transaction in farming products.

### 2.3. Risks or Catastrophes Associated with Farming Products and its Impact on Farming Product Secured Transaction

The agricultural sector in Ethiopia has suffered many catastrophes so far. We have witnessed that this sector has been a victim of different catastrophes at different times.<sup>118</sup> It has been a victim of serious drought and floods.<sup>119</sup>“The country has long history of recurring droughts, which have increased in magnitude, frequency, and impact since the 1970s.”<sup>120</sup> Because of such droughts,

---

<sup>116</sup>Movable property Security Rights Proclamation, supra note 3, Art. 7.

<sup>117</sup>Henry Deeb Gabriel, ‘The New Zealand Personal Property Securities Act: A Comparison with the North American Model for Personal Property Security’, 34 *The International Lawyer*4, 1123(2000), at 1128.

<sup>118</sup>Temesgen Tadesse Deressa, *Assessment of the vulnerability of Ethiopian agriculture to climate change and farmers’ adaptation strategies*, PhD Thesis, Faculty of Natural and Agricultural Sciences, University of Pretoria, (2010), at 18

<sup>119</sup>*Ibid.*

<sup>120</sup>The World Bank Group, ‘Climate Risk Profile: Ethiopia’, (2020), at 10.

farmers have been losing their crop and livestock productions.<sup>121</sup> Besides, in some cases, their livestock becomes a victim of livestock diseases.<sup>122</sup> As a study shows, livestock in Ethiopia is experiencing a severe livestock disease that surges from time to time.<sup>123</sup> This shows that agricultural products are highly exposed to risk or natural catastrophes.

Because of this, lenders need to protect their interest in requiring borrowers (smallholder farmers) to buy an insurance policy for such collaterals, and it is called borrower-placed collateral insurance.<sup>124</sup> If the borrower buys an insurance policy for farming product collateral, the interest of the creditors on the collateral is secured. In such a case, the lender can proceed against the insurance company provided the collateral is damaged or lost. However, the borrower may not buy insurance for the collateral. In such a case, the lender may buy an insurance policy for the collateral, and we call this lender/creditor-placed insurance, collateral protection insurance, or forced-placed insurance.<sup>125</sup> Lender-placed insurance means “a policy that is ultimately meant to protect the lender from uninsured losses and will not typically provide coverage for the borrower’s personal property.”<sup>126</sup> By using force-placed collateral insurance, the lender secures its interest over the collateral for the event that the collateralized property is damaged or lost.<sup>127</sup> Of course, even in lender-placed insurance, the ultimate cost rests upon the borrower, as the lender will add it to the loan. Lender-placed collateral insurance is costly compared with borrowers-placed insurance.<sup>128</sup> Hence, ensuring the collateral through a lender-placed insurance system exposes the borrower to a higher premium cost.

---

<sup>121</sup>*Ibid* at 11 &12.

<sup>122</sup>The Association of Ethiopian Microfinance Institutions (AMFI), ‘The Potential for High-Value Livestock Indemnity Insurance in Ethiopia’s Oromia Region’, 41-42 (2010).

<sup>123</sup>*Ibid*.

<sup>124</sup>Jennifer Ifftetal, ‘Farm Debt Use by Farms with Crop Insurance’ (2013) 28 (3)The magazine of food, farm, and resource issues’, <<http://www.choicesmagazine.org/choices-magazine/theme-articles/current-issues-in-risk-management-and-us-agricultural-policy/farm-debt-use-by-farms-with-crop-insurance>>last accessed on December 20, 2019.

<sup>125</sup>First Service Corporation, ‘Lender-Placed Insurance’, <<http://www.fscinsurance.com/lender-placed-insurance>>last accessed on December 23 2019.

<sup>126</sup>*Ibid*.

<sup>127</sup>*Ibid*.

<sup>128</sup>Julia Kagan, ‘Force Place Insurance’, <<https://www.investopedia.com/terms/f/forced-place-insurance.asp>>last accessed on December 23, 2019.



As the previous studies show though farmers in Ethiopia are willing to insure their agricultural products, their income level becomes a restraint.<sup>129</sup> The practice shows that farmers are reluctant to buy a collateral insurance policy since their income does not allow them to pay the premium. For example, research conducted in Tigray Regional State shows that the interests of a farmer to pay weather index insurance premium decreased while there is a decrease of subsidies in the premium payment.<sup>130</sup> According to this study, farmers insist on insuring their agricultural products without subsidies.<sup>131</sup> This shows that farmers cannot afford to pay the insurance premium by themselves. The effect is that the farmer will not get access to credit unless there is some subsidy to buy collateral insurance.

Besides, previous studies show that the reality of the country is not conducive enough for insurance companies to provide insurance services for smallholder farmers. There is no updated and accurate data in the country for assessing the potential risks in the property to be insured.<sup>132</sup> For example, the National Metrological Agency does not publicize the weather index data in the country timely and accurately.<sup>133</sup> Because of this, insurance companies cannot able to assess the imaginable risks of weather insurance to provide weather index insurance to smallholder farmers.<sup>134</sup> Besides, studies show that insurance companies even hesitate to implement agricultural insurances fearing the losses since agricultural insurance is the riskiest one.<sup>135</sup> Moreover, as farmers are residing in rural areas that lack adequate infrastructures, it is difficult for insurance companies to assess the potential risks attached to the property insured and to supervise the insured property. Generally, the existence of high risks associated with farming products, the inability of farmers to pay a collateral insurance premium, and the challenges to insurance companies to provide the service are prospective barriers to a farmer getting funds from lenders using farming products collateral.

---

<sup>129</sup>A. Wong, ‘Weather insurance for Ethiopian farmers’, <<https://includeplatform.net/publications/final-findings-weather-insurance-for-ethiopian-farmers/>> last accessed on December 24, 2019.

<sup>130</sup>*Ibid.*

<sup>131</sup>*Ibid.*

<sup>132</sup>Eyob Miherette, “Providing weather index and indemnity insurance in Ethiopia”, <<https://agroinsurance.com/en/10839/>> last accessed on December 25, 2019.

<sup>133</sup>*Ibid.*

<sup>134</sup>*Ibid.*

<sup>135</sup>Nahu Senaye, ‘Weather Insurance for Farmers: Experiences from Ethiopia’, Conference on New Directions for Smallholder Agriculture, Rome, 12 (2011).

## Concluding Remarks

In August 2019, Ethiopia passed a new proclamation on movable property security rights that bring wide-ranging rules on security rights in movable properties. This Proclamation broadens the type of movable properties that can be granted as collateral. Farming products are properties, among others, that the proclamation lists as property to be given as collateral. A person can use farming products including but not limited to crop grown, growing or to be grown, forest, timber, and other wood products, livestock, born or unborn, bees and poultry, and the produce and progeny thereof, supplies used in the farming operation, or products of livestock in their unmanufactured states as collateral to secure the interests of a creditor. The main reason for expressly allowing using the farming products as collateral is to enable farmers to access credit easily.

Though the proclamation intends to increase access to finance for farmers, this paper argues that farming product secured transactions will face some challenges to be practiced as much as the proclamation intends. This is because, first, most farming product collaterals, other than products stored in a warehouse, are not conducive to perfect the interests of secured creditors. To inform other potential creditors adequately, the farming product collateral in which a security interest is created shall be described in ‘a manner that reasonably allows their identification.’ For example, according to the NBE directive on codification, valuation, and registration of movable property collaterals, livestock collateral is required to be described using the plastic tag number supplied by the Ministry of Agriculture. However, the ear tag number is not adequate to inform other potential creditors as it may be damaged; cut-off, or intentionally detached by the owner. To avoid this problem, it is better to create a security interest over all livestock of the debtor or, at least, in a specific category of livestock. If the collateral is a crop, it is required to be described using the tax identification number of the owner, the unique parcel identification number of the landholding certificate of the person who offered it as collateral for the credit; the type of crop being pledged, the expected maximum output and the maximum output to be pledged for credit. Nevertheless, it is difficult to describe crops since most crops are located in remote areas. Loan officers may not be able to go by foot a long distance for getting information for description. An improvement of infrastructures shall be made in the rural areas in order to put into action the crop collateralized secured credit in the country.

Second, the total prohibition of grantors to sell the collateralized farming product destructs the marketability of the product in the market. Potential buyers would be discouraged to buy farming products fearing the claim of secured creditors. The law does not even favor those buyers who buy the collateral 'in the ordinary course of the seller's business and without the knowledge that the selling of the collateral violates the lender's interest. Rationally, this restricts the marketability of the farming products as buyers are always at risk for their right in the farming product is subordinate to the secured creditor's right even when they buy the product in the ordinary course of the seller's business. Therefore, in order to avoid these problems, the NBE directive needs to provide an exception to the priority right of secured creditors. Exceptionally, it should make the rights of secured creditor subordinate to the buyer of the farming product in the ordinary course of the seller's business. This facilitates transactions in farming products.

Third, the farming product secured transaction is impracticable due to risks or catastrophes associated with farming products. Farming products in Ethiopia are exposed to catastrophes or risks. They may be a victim of drought, flood, or other natural or synthetic risks. In such cases, the farmer will lose the collateralized farming products, which, in turn, result in the loss of the right to the lender, in case there is a default of the debtor. This problem, of course, can be minimized by insuring the collateral. Nevertheless, the problem in insuring the collateral is that it increases the cost of a loan to borrowers. A farmer may not afford to pay an insurance policy premium. Most of the Ethiopian farmers are farming in a subsistence way. Therefore, expecting them to cover the collateral with an insurance policy would be absurd. They apply for a loan because of the scarcity of capital to fund their agriculture. They would not apply for a loan, had they had a fund to purchase an insurance premium. Actually, lenders can buy an insurance policy for the collateral through a forced or lender-placed insurance system. Yet, the farmer assumes the cost by adding on the loan. Even, it is challenging to insurance companies to provide insurance services for remotely located farming products as it is challenging to evaluate and monitor potential risks and supervise the insured property.

## Bibliography

### Article

- Asress Adimi Gikay, 'Rethinking Ethiopian Secured Transactions Law through Comparative Perspective: Lessons from the Uniform Commercial Code of the US', 1 Mizan Law Review 11, (2017).
- Atkilt Admasu and Issac Paul, Assessment on the Mechanisms and Challenges of Small Scale Agricultural Credit from Commercial Banks in Ethiopia: The Case of Ada'a Liben Woreda Ethiopia, Journal of Sustainable Development in Africa, (2010), Vol.12, No.3
- Barkley Clar, 'Secured Transactions', 4 the Business Lawyer 42, (1987).
- Daniel P Johnson, 'Federal Legislation Provides Protection for Buyers of Farm Products: Food Security Act Supersedes the Farm Products Exception of UCC Section 9-307(1)', 47 U Pitt L Rev 749, (1986).
- Doreen Auma and Philip Ahen Mensah, *Determinants of Credit Access and Demand Among Small-Holder Farmers in Tigray Region, Ethiopia*, Norwegian University of Life Sciences School of Economics and Business, Master's Thesis, (2014).
- Iyare Otabor-Olubor, *A Critical Appraisal of Secured Transactions over Personal Property in Nigeria: Legal Problems and a Proposal for Reform*, (Ph.D. dissertation, Nottingham Trent University 2017).
- Keith G Meyer, 'A Garden Variety of UCC Issues Dealing with Agriculture', 58 U Kan L Rev 1119, (2010).
- Keith G Meyer, 'Current Article 9 Issues and Agricultural Credit', 10 Drake J Agric L 105, (2005).
- Keith G. Meyer, 'The 9-307(1) Farm Products Puzzle: Its Parts and Its Future', North Dakota Law Review 60, (1984).
- Marek Dubovec & Cyprian Kambili, *A Guide to the Personal Property Security Act: The Case of Malawi*, Pretoria University Law Press, (2015).
- Nahu Senaye, 'Weather Insurance for Farmers: Experiences from Ethiopia', Conference on New Directions for Smallholder Agriculture, Rome, (2011).
- Nebiat Tekle, *Bank Credit to the Agricultural Sector in Ethiopia: A Trend Analysis*, MSC thesis, ST. Mary's University School of Graduate Studies, (2017)
- Obse M. Eshetu, *Determinants of credit constraints in Ethiopia*, Master's Thesis in Economics, Norges Arktiste University, (2015)
- Ronald J. Mann, 'Explaining the Pattern of Secured Credit', 3 Harvard Law Review 110, (1997).
- Steve, Weise & Stephen, L. Sepinuck, 'Personal Property Secured Transactions', 4 the Business Lawyer 68, (2013).
- Steven O. Weise, 'Personal Property Secured Transactions', 4 the Business Lawyer 64, (2009).
- Temesgen Tadesse Deressa, *Assessment of the vulnerability of Ethiopian agriculture to climate change and farmers adaptation strategies*, PhD Thesis, Faculty of Natural and Agricultural Sciences, University of Pretoria, (2010)
- The Association of Ethiopian Microfinance Institutions (AMFI), 'The Potential for High Value Livestock Indemnity Insurance in Ethiopia's Oromia Region', (2010).
- The World Bank Group, 'Climate Risk Profile: Ethiopia', (2020)

- Thomas H. Jackson & Anthony T. Kronman, ‘Secured Financing and Priority among Creditors’, 6 Yale Law Journal 88, (1979).
- Xuan-Thao Nguyen & Bich T. Nguyen, ‘Transplanting Secured Transactions Law: Trapped in the Civil Code for Emerging Economy Countries’, 1 North Carolina Journal Of International Law And Commercial Regulation 40, (2014).
- ገዙ አየላ መንግስቱ፣ የኢትዮጵያ የባንክ እና የሚተላለፉ የንግድ ሰነዶች ሕግ, (2009))

### Laws

- Civil Code of the Empire of Ethiopia, 1960, *Negarit Gazzeta* ( Extraordinary issue), Proc. No. 165, 19<sup>th</sup> year, No. 2
- Commercial Code of the Empire of Ethiopia, (1966), *Negarit Gazzeta* (Extraordinary issue), Proc. No. 166, 19<sup>th</sup> year, No. 3
- Movable property security rights proclamation, (2019), Fed. Neg. Gaz., Proc. No. 1147, 25<sup>th</sup> year, No. 76
- National Bank of Ethiopia, Codification, Valuation and Registration of Movable Properties as Collateral for Credit, Directive No. 186/2020
- National Bank of Ethiopia, Operationalization of Collateral Registry, Directive No. MCR/01/2020
- Uniform Commercial Code of USA

### Internet

- New Business Ethiopia, ‘Ethiopia’s smallholder farmers to use cattle as collateral’, <https://newbusinessethiopia.com/finance/ethiopias-smallholder-farmers-to-use-cattle-as-collateral/>>
- Ali Khan, ‘Secured Transaction Final review 2012’, <<https://www.youtube.com/watch?v=-Tk-eO13blk&t=320s>>
- First Service Corporation, ‘Lender-Placed Insurance’, <<http://www.fscinsurance.com/lender-placed-insurance>>
- Julia Kagan, ‘Force Place Insurance’, <<https://www.investopedia.com/terms/f/forced-place-insurance.asp>>
- Jason Gordon, ‘Perfection of a Security Interest’, <<https://thebusinessprofessor.com/lesson/perfection-of-a-security-interest/>>
- A. Wong, ‘Weather insurance for Ethiopian farmers’, <<https://includeplatform.net/publications/final-findings-weather-insurance-for-ethiopian-farmers/>>
- Eyob Miherette, “Providing weather index and indemnity insurance in Ethiopia”, <<https://agroinsurance.com/en/10839/>>
- Jennifer Ifftetal, ‘Farm Debt Use by Farms with Crop Insurance’ (2013) 28 (3)The magazine of food, farm, and resource issues <<http://www.choicesmagazine.org/choices-magazine/theme-articles/current-issues-in-risk-management-and-us-agricultural-policy/farm-debt-use-by-farms-with-crop-insurance>>
- New Business Ethiopia, ‘Ethiopia’s smallholder farmers to use cattle as collateral’, <https://newbusinessethiopia.com/finance/ethiopias-smallholder-farmers-to-use-cattle-as-collateral/>>