

**ELECTRONIC WAREHOUSE RECEIPTS FOR AGRICULTURAL
PRODUCTS**

(presented by Dr. David P. Stewart)

Mandate

The Inter-American Juridical Committee decided by consensus at its meeting held on August 9, 2012, during its 81st regular session, CJI/RES. 196 (LXXXI-O/12), under the powers vested in it in Article 12, c) of its Statutes, to include on the agenda for its next session the study of electronic warehouse receipts for agricultural products with a view to determining whether it might usefully contribute to the discussion of this subject through the subsequent development of a set of recommended principles or a model law. At that same meeting, a rapporteur was appointed to submit a preliminary document to the Juridical Committee for analysis and debate.

Context

In many countries, the agricultural sector continues to be dominated by small-scale operations in which a majority of producers cultivate only a few hectares and lack ready access to financial credit. In such situations, producers are often forced to sell their fruits, vegetables and other crops immediately after harvest in order to get money to pay expenses and to buy supplies for the next planting.

The sale of produce immediately after harvest can saturate the market, leading to low prices. Farmers may be forced to accept these low prices because they cannot get financing from commercial banks, which view them as high risk. Without loans, farmers are not likely to be able to pay for storage at warehouses. Moreover, warehouses are often located far from the farms and transportation costs can be high for distant producers.

Improving the performance of the agricultural sector is critical for economic growth and poverty reduction in many regional economies. A system is needed that enables farmers to store some of their grain after harvest and to use it as collateral for loans based on the market value of their commodities, thus generating funds to cover immediate expenses and to help prepare for the next harvest. Assured of financing, farmers can wait for market prices to improve before selling their products. As a result, they can obtain a higher average price, which in turn will increase their annual incomes.

Definition and Benefits

Warehouse receipt financing is a form of asset-based lending that allows farmers, producers, and traders of agricultural commodities to obtain bank loans by pledging their warehouse receipts issued against commodities deposited in warehouses. Warehouse receipts are issued by accredited warehouses to farmers and traders; the receipts serve to acknowledge the quantity and quality of the produce deposited with the warehouses. On the basis of these receipts, the farmers can raise money from banks willing to accept the receipts as collateral.

A warehouse receipt serves as a document of title and provides proof of ownership of a specific quantity of products with specific characteristics and stored in a specific warehouse goods held in inventory. When issued in negotiable form and backed by the necessary legal guarantees, it gives the holder the right to transfer ownership while the goods are still in the possession of the warehouse. It can also serve as collateral, and can be sold, traded or used for delivery against financial instruments including futures contracts.¹

An effective warehouse receipt system can help farmers obtain access to better credit and avoid distress sales as well as safeguard financial institutions by mitigating risks inherent in extending credit to farmers. It can also help to increase the overall efficiency in the relevant commodity market, smoothing the supply and prices in the market, improving incomes and reducing losses.

A modern *electronically-based* system of warehouse receipts can significantly increase the speed of transactions without increasing the risk, thereby permitting small producers (especially those who produce perishable commodities) to participate in markets much farther from their own locations.

Initiatives/Examples

Warehouse receipts systems have been implemented in recent years in Poland, Hungary, Slovakia, Bulgaria, Turkey, Indonesia, Uganda, Ghana, and South Africa, to name a few. In Ukraine, the European Bank for Reconstruction and Development (EBRD) funded a Grain Warehouse Receipt Program aimed at creating the necessary legal environment for a grain warehouse storage and receipt program to function.

In Ethiopia, a Warehouse Receipts Financing Initiative of the International Financial Corporation (IFC) has helped to expand access to financing for farmers, traders, and cooperatives and develop agricultural commodities markets since 2009. The Initiative has increased the availability of warehouse receipt financing

¹. Generally, see WORLD BANK. **Expanding Post-Harvest Finance through Warehouse Receipts and Related Instruments.** *Agricultural and Rural Development Notes*, n.8, March 2006; USAID. Warehouse Receipts: Financing Agricultural Producers. *Technical Notes*, n. 5, Oct. 2000. Available at: <http://pdf.usaid.gov/pdf_docs/PNACQ697.pdf>.

in the country. A symposium on the program was held in Addis Ababa in June 2012.

In India a new Warehousing (Development and Regulation) Act, 2007 came into effect in 2010. The Act makes warehouse receipts negotiable.

In the United States, warehouse receipts are supported by federal legislation, the Warehouse Receipts Act of 2000, which replaced a legislation enacted in 1916.² It permits the issuance and use of EWRs. By the end of the 1990s, almost 90% of all stored cotton had been covered by electronic warehouse receipts. One of these issuers, eGrain, established in 2006, facilitated the issuance of EWRs for grain and rice worth over USD \$3 billion.

The Problem

In a number of countries in Central and South America, the practice continues in general to be based on a dual set of documents issued by the warehouseman. The documents are (1) the pledge certificate (*certificado de prenda*), also referred to in some jurisdictions as an ownership certificate (*certificado de propiedad*) or title of ownership (*titulo de propiedad*) and (2) the pledge bond (*bono de prenda*).

The first of these documents (the pledge certificate) is supposed to act as a receipt for the stored goods; it is issued by the warehouseman in the name of the depositor as owner of the deposited goods. This certificate (receipt) is also supposed to stay with the depositor until the goods are ready to be retrieved by him or by his assignee or pledgee. The second document (the pledge bond) is designed to be endorsed or delivered *stet* by the depositor to the financier upon receiving the latter's loan. With that pledge bond the holder (usually a bank) can claim the goods from the warehouseman provided that their depositor also releases them by delivering his certificate of pledge or of ownership.

However, this method of securing loans is clearly unsuited for an increasingly faster logistical chain. Today, for example, many agricultural products are moved quickly after harvest to warehouse "A," where they remain for only a few hours or days before being sent toward their destination. From "A" they might be taken to warehouse "B" and stored briefly before being put into a container and placed on board an ocean-going vessel, or an airplane, a truck or railroad car and sent to a foreign destination. Upon arrival, a similar sequence of storage and transportation may take place. It is clearly inefficient to require the release of a certificate of ownership or of deposit from a distant depositor or bailor each time the endorsement of pledge bond is made by its latest holder in a different location or country. Doing this in paper form is even more inefficient.

². The Federal Warehouse Receipts Act, Aug. 11, 1916, c. 313, Pt. C, § 2, as amended Nov. 9, 2000, Pub.L. 106-472, Title II, § 201, 114 Stat. 2061, codified at 7 U.S.C. 241-277.

While documentary trade instruments have historically not been common in Central and South America, several countries have introduced modern warehouse receipts systems in recent years, including Argentina and Brazil. In addition, some jurisdictions in the hemisphere have begun using electronic warehouse receipts (hereinafter EWR). Brazil, for example, adopted laws and regulations conducive to the issuance and transfer of EWRs called certificates of deposit and warrants. Brazilian Law No. 11.076 of December 2004 authorized the issuance of agribusiness certificates of deposit and agribusiness warrants, and has even created a clearing system for warehouse receipt transactions, although its electronic receipts for some unexplained reason continues to rely on two paper based or electronic documents, messages or records.

Mexico sought to enact a new warehouse receipt law in 2008 that still relied on the two document method, even though it has become abundantly clear that a single document or electronic message or record is the most effective and safe method of conveying possessory interests in the stored collateral.

Pre-Conditions

An effective warehouse receipts system can reduce uncertainty and increase efficiency in agricultural markets. But its success depends on several pre-conditions. Clearly, a surplus of the relevant commodities must exist (otherwise, there can be no products for the producer to sell). There must also be accessible markets (otherwise, there can be no place for the producer to sell). The necessary infrastructure must exist to connect the producer to the markets (specifically, warehouses and an effective transportation system).

Banks must be prepared to offer the necessary financing. This, in turn, requires a reliable legal structure which establishes and regulates the system of warehouse receipts and guarantees the enforceability of the receipts in case of default. Without credibility among financial institutions, a warehouse receipts scheme is worthless because it cannot help farmers to get a loan. Besides mandating the negotiability of warehouse receipts, the system must also prescribe the form and manner of registration of warehouses and issue of negotiable warehouse receipts, including the legitimacy of electronic records and transfers.

The system must also provide effective government monitoring and oversight. Warehouses must be inspected and licensed (by governmental agencies or non-governmental bodies such as trade groups) according to established standards, and some form of regulatory authority is needed to protect the interests of holders of warehouse receipts against negligence, malpractices and fraud.

The Legal Framework

The legal framework for an effective system of electronic warehouse receipts must rest on two pillars. First, it must recognize modern forms of secured

transactions and methods of secured financing, including negotiable warehouse receipts. Second, it must recognize and give effect to electronically-created and stored records on the same basis as paper records.

(1) *Secured Transactions*. Within the OAS, the basis for an effective system of secured financing already exists, in the 2002 OAS Model Law on Secured Financing. The text of that Model Law is available at http://www.oas.org/dil/CIDIP-VI-securedtransactions_Eng.htm. Prepared within the CIDIP-VII process, the Model Law provides the necessary legal framework for domestic implementation. In particular, it provides in Article 1 that a State which adopts the Model Law “shall create a unitary and uniform registration system applicable to all existing movable property security devices in the local legal framework, in order to give effect to this Law.” A central registry serves the critical purpose of standardizing the documentation required to provide proof of title to the property in question, which is a critical step in establishing it as acceptable collateral for bank lending.

The Model Law has been supplemented by the OAS Model Registry Regulations, which were prepared and approved by CIDIP-VII on October 9, 2009.³ A number of countries in the hemisphere, including Peru, Guatemala, and Honduras, have enacted modern secured transactions laws (*Ley de Garantías Mobiliarias*). In 2010 Mexico put into operation its moveable assets registry (*Registro Único de Garantías*).⁴

(2) *Electronic records*. Traditionally, paper receipts have been used as evidence of ownership, deposited at banks to cover financing activities and held as collateral against the transaction. But paper documents are cumbersome, costly and inefficient, especially since they must be physically transferred between the growers, the warehouses, the banks or other lien holders, etc. Electronic warehouse receipts eliminate the need to store paper files. They are safer, faster and more economical. It is therefore important to remove any legal barriers that might prevent the legally effective use of electronic communications.

The importance of electronic communications was in fact recognized in Article VII of the OAS Model Law, which states that the written security contract “may be manifested by any method of communication that leaves a permanent

³. CIDIP-VII/RES.1/09 rev.2, OEA/Ser.K/XXI.7. Resolution available at: <http://www.uncitral.org/pdf/english/colloquia/3rdSecTrans/John_Wilson_MR.pdf>.

⁴. Generally, see KOZOLCHYK and WILSON. **The New Model Law on Secured Transactions**. *Uniform Law Review*, n. 262, 2002; WILSON. **Model Registry Regulations under the Model Inter-American Law on Secured Transactions**. *Uniform Law Review*, n. 515, 2010; KOZOLCHYK. **Implementing the OAS Model Law in Latin America: Current Status**. *Arizona J. Int'l Comp*, n. 28, L. 1, 2011; AKSELI, Orkun. **International Secured Transactions Law: Facilitation of Credit and International Conventions and Instruments**. Routledge, 2011.

record of the consent of the parties to the creation of the security interest, including telex, telefax, electronic data interchange, electronic mail, and any other optical or similar method, according to the applicable norms on this matter and taking into account the Resolution of this Conference attached to this Model Law (CIDIP-VI/RES. 6/02).”

In this regard, reference should also be made to the Uniform Inter-American Rules for Electronic Documents and Signatures (October 3, 2001).⁵ These rules were adopted in light of the development of the Model Law and were intended to provide basic enabling provisions for electronic transactions to assist OAS Member States in preparing standardized commercial documentation for international transportation.

While electronic record-keeping is now recognized and endorsed in principle in various international instruments, there is general agreement that more specific and detailed rules are required to implement those principles in specific economic sectors. For example, the 2005 UN Convention on the Use of Electronic Communications in International Contracts does set out a general rule of “functional equivalence,” but by its explicit terms it does not apply to warehouse receipts. The 2008 UN Convention on Contracts for the International Carriage of Goods Wholly or Partly by Sea (the “Rotterdam Rules”) also recognizes the validity of electronic communications in the area of ocean transport, including “negotiable electronic transport records,” but its success will of course depend on effective domestic implementation.

More recently, UNIDROIT has begun to consider the role of a modernized agricultural financial system in the development of sustainable and profitable agricultural markets.⁶

UNCITRAL has taken the lead in addressing the need for countries to modernize their laws by accepting electronic communications as the equivalent of written communications. In 1996, UNCITRAL adopted a Model Law on Electronic Communications, which together with its subsequent Guide to Enactment provide a basis for modernization of domestic law. A number of countries around the world have in fact relied on the 1996 Model Law in whole or in part. Among others, Canada, Australia, Korea, Japan, the United States and Columbia have updated their laws in recent years.

⁵ Available at:

<http://www.oas.org/dil/CIDIPII_topics_futures_cidips_electroniccommerce_signatures_3oct2001.htm>.

⁶ See GABRIEL, Henry Deeb. **Warehouse Receipts and Securitization in Agricultural Finance.** *XVII Uniform Law Review*, UNIDROIT, n.369, 2012.

Most recently, the discussion has continued in UNCITRAL's Working Group IV on electronic commerce. In August 2012, the Governments of Columbia, Spain and the United States submitted a paper on the legal issues relating to the use of electronically transferable records. See UN Doc. A/CN.9/WG.IV/WP.119 (Aug. 3, 2012) (copy attached).⁷

In paragraph 48, that paper specifically addressed the advantages and benefits of electronic warehouse receipts for agricultural economies. As indicated in the official report of the Working Group's October 2012 meeting, consideration is being given to the preparation of a model law on electronically transferable records, and the Working Group will again discuss the matter at its next meeting in May 2013.⁸

Recommendation

The Inter-American Juridical Committee may wish to consider how it might best contribute to the development of an effective system of electronic warehouse receipts in the hemisphere, for example by preparing (i) a set of draft principles for consideration in the formulation of a model law on the subject of electronic warehouse receipts, or (ii) the text of a draft OAS Model Law.

It may also wish to consider conducting a survey of Member States of the OAS regarding their law on secured transactions and electronically transferrable records, based on the relevant OAS and international instruments.

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⁷. Available at:
<http://www.uncitral.org/uncitral/en/commission/working_groups/4Electronic_Commerce.html>.

⁸. See UNCITRAL. **Report of the Working Group IV (Electronic Commerce)**. 46th session, Vienna, 29 October-2 November 2012, UN Doc. A/CN.9/761 (Nov. 5, 2012). Available at:
<http://www.uncitral.org/uncitral/en/commission/working_groups/4Electronic_Commerce.html>.

