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*Implementation of a System of Licensed Public Warehouses
and Warehouse Receipts in Bulgaria*

*By Krassimir Kiriakov
Country Representative
ACDI/VOCA, Bulgaria-Sofia*

INTRODUCTION

In July 1997 a team of Bulgarian and American experts completed a survey of the grain production and processing industry in Bulgaria. The survey was sponsored by USAID through FLAG Consortium. The main goal of the survey was to analyze the situation in the grain sector, identify major problems and constraints and recommend a plan for assistance. There were 32 issues that were identified by consensus from all the groups participating in the survey. In this presentation we are going to mention 9 of them:

1. Lack of trade rules and developed infrastructure of the domestic market and for access of the international markets
2. Very high price of quality seeds
3. High price of agricultural inputs
4. Lack of reliable grain storage facilities in the smaller production units and limited choice for reliable grain storage
5. Lack of reliable standards for quality of grain
6. Lack of access to commodity markets
7. Very limited access to short term financing for operational capital
8. Lack of information about sources of financing
9. Lack of access to reliable grain marketing information

The reason that we selected the above mentioned problems is that we see the Warehouse Receipt System as an alternative solution to these constraints and a focus point for more comprehensive approach that provides general development of the grain industry in Bulgaria.

At the initial stage of development of the WHR system in Bulgaria, two major constraints for the producers and processors and traders of grain were identified. One was the access to short term financing for operational capital. The financial institutions in Bulgaria were still very conservative in their short term lending policies and the requirements for collateral for such credits are not achievable for the majority of small and medium size producers and processors. The second problem was lack of regulated and guaranteed system of grain storage, where depositors can safely store their products and wait for the best market price.

The importance of the grain industry in Bulgaria for the overall agricultural development and the consensus between The Government of Bulgaria and all the international donors as USAID, The World Bank, IMF and EBRD for the need of restructuring of the grain market provided favorable conditions for the implementation of Grain Industry Development Program, funded by USAID and implemented by the cooperative efforts of ACDI/VOCA and USDA.

The Major components of The Program are:

1. Development and Implementation of WHR system in Bulgaria.
2. Development of grain commodity markets.
3. Assistance to providers of grain marketing information.

4. Assistance to the trade organizations in the grain industry in their efforts to consolidate and influence policy decisions and establish trade rules.
5. Technical assistance and training to private grain processing and storage companies.

WHR SYSTEM AS AN ALTERNATIVE SOLUTION FOR THE PROBLEM OF ACCESS TO SHORT TERM FINANCING AND SECURE STORAGE

The main program objective is to introduce the WHR system as an alternative solution for grain producers and processors to provide short term financing for their operations, using grain as collateral.

A well-developed system of licensed public warehouse and the use of warehouse receipts for storage and marketing of grain provides the following advantages that contribute to the overall development of the grain industry:

1. Provides uniformed and well-regulated system for storage of grain.
2. Provides protection for the depositors of the grain insuring the quality and the quantity of the deposited grain.
3. Introduces the use of warehouse receipts, which are official documents for ownership and can be used as collateral for short-term loans.

The concept of a WHR system is based on the use of grain storage licensed as public warehouses. These warehouses receive the right to store grain of third parties and issue warehouse receipts. Receiving the license the warehouse bears the responsibility to constantly provide a high level of technical and financial performance. This is one of the ways to create confidence in the depositors that their grain would be stored with guaranteed quality and quantity. Public warehouses should be situated in large production areas; important marketing centers or nears import-export terminals.

The warehouse receipts that are issued by the public warehouses are used for implementation of comparatively simple mechanism for using grain as collateral for short term financing. The producers and processors are given the opportunity to be flexible in using the grain they own as collateral and to determine the best time to market the grain. The use of warehouse receipts makes the transfer of ownership between the seller and buyer easier and quicker, avoiding the need for physical relocation of the commodity.

The financial institutions, which accept warehouse receipts as collateral are able to reach a higher level of liquidity of the pledge and gain the right to claim this collateral before other creditors. The banks also have the advantage of higher level of protection of the collateral enforced by both the good management practices of the licensed public warehouse and the supervision of the regulatory agency.

A well operating warehouse receipt system is based on appropriate legislation that enables a regulatory agency to execute control of the key components of the system. The existence of clear and secure licensing procedures contributes to the creation of trust in the system. The legal framework should be designed in such a way that provides clear definitions for the rights and responsibilities of all participants in the system.

LEGAL FRAMEWORK AND TECHNICAL ASPECTS OF THE IMPLEMENTATION OF WAREHOUSE RECEIPT SYSTEM IN BULGARIA

The idea for development of a warehouse receipt system in Bulgaria was formalized on July 29, 1998, after the Parliament passed the new law for the marketing and storage of grain. This event was an important step forward after a six months public discussion among representatives of the grain industry – producers, processors and traders, bankers and experts from the Ministry of Agriculture and the Agricultural commission in the Parliament. The importance of the discussion for the future development of the grain industry in Bulgaria was backed up by the personal involvement of the Minister of Agriculture and the Head of the Parliamentary Agricultural Commission. The Grain law contains the legal framework that provides conditions for the implementation of the warehouse receipt system and defines the rules and regulations for the marketing and storage of grain. The document also describes the authority of the government institutions that regulate this process as well as the rights and responsibilities of the physical persons and legal entities involved in the storage and marketing of grain.

The main goals of the Grain Law are:

1. To create conditions for sustainable development of the production and processing of grain in Bulgaria.
2. To provide stability for the grain market in the country.

In that respect the successful implementation of a warehouse receipt system contributes to the accomplishment of both goals.

I. Public Warehouses and Grain Storage

The Grain Law regulates two types of business entities, involved in the storage of grain – Public Warehouses and Grain Storage, both of which are due to licensing procedure. The licensed grain storage is not entitled to issue warehouse receipts, that is why it is not going to be included in our presentation.

A licensed Public Warehouse for storage of grain according to the Bulgarian legislation is a sole proprietor (trader) with main business activity storage of deposited grain and issuing of warehouse receipts as well as joint stock companies and limited liability companies registered under the Commercial Law. The major licensing requirements for a public warehouse are as follows:

1. Minimum required capital for incorporation of a public warehouse for grain – 100 000 BGL (55 000 USA\$).
2. The public grain warehouse should have a minimum storage capacity of 3000 MT.
3. The public grain warehouse provides bank deposit or irrevocable bank guarantee for 10 BGL (5.5 USA\$) per metric ton capacity at the disposition of the Ministry of Agriculture. The expiration of the deposit or the bank guarantee can not be earlier than two months after the expiration of the license for public warehouse.
4. The public grain warehouse cannot be a creditor or provide guarantees for credits for a third party.

5. The public grain warehouse is required to insure the grain storage against fire, flood and earthquake.
6. The public grain warehouse is required to announce in a public place the storage fees.
7. The public grain warehouse is required to provide to the National Grain Service information for about its business operation.

Besides the above-mentioned major requirements, the public grain warehouse has to meet several technological standards as well as prove its financial stability.

All these requirements create **the first level for protection of the system** and create conditions, under which the licensed Public Grain Warehouses can be reliable participants, thus providing guarantees for appropriate storage of the grain of respective quality and quantity. This condition is very important for the depositors and for the financial institutions that will accept this grain as collateral. The performance of the public warehouse is crucial for the smooth operation of the system. The Grain law regulates the creation of **a second level for protection of the system**. Within one year from the acceptance of the law in the parliament, the public warehouses should form an indemnity fund, which guarantees their performance. This issue is of utmost importance for the system as a whole. There are several approaches used in other countries for secondary guarantee of the performance of the public grain warehouses. One of the most popular approaches also broadly used in USA is the insurance bond, purchased by the warehouse and kept by the licensing authorities. This insurance bond covers partly the risks of the depositors related to the improper performance of the public warehouse. Another approach for creating a performance guarantee is the accumulation of an indemnity fund that protects the interests of the depositors. It is also possible to have a combination of indemnity fund and insurance bonds with well-defined mechanism of payments of the claims. There are several basic principles that should be followed. The indemnity fund should be privately financed and managed and administered with active participation of the private sector and reliable insurance companies should issue the insurance bond. The premium of the insurance bond should be affordable by the industry and at the same time reflect the risk level in Bulgaria.

Further analysis of the most appropriate instruments for financial guarantees focused the efforts on establishment of indemnity fund as a second level of protection of the system. In the spring of year 2000, the Minister of Agriculture approved the statute of Indemnity Fund “ Grain “.

The two levels for protection of the system that has been described should be well accepted by the financial institutions. Both levels are targeted towards the secure existence of the collateral. The banks that accept warehouse receipts should trust the public warehouses that have issued them and feel comfortable with the technical and financial conditions for storage of the grain used as collateral. Until the system is implemented on a large scale and all the participants have proved their performance we recommend that the banks come up with ways to execute parallel control of the public warehouses using their own specialists for informal inspections.

II. Warehouse Receipt

The warehouse receipt is the next very important component forms the system. Warehouse receipts vary in different countries by format and structure but by all means they should be comparatively simple document based on strong legislation. If they provide simple mechanism for transfer of ownership or initiating a pledge, they become a very well accepted and commonly used tool.

The Bulgarian legislation describes the warehouse receipt as a promissory security issued by a public warehouse and proves the deposition of grain and the obligation of the warehouse to deliver the grain to the legitimate holder of the receipt. The warehouse receipt is defined in the Commercial Law. There are several important specifications added to this definition that concern the warehouse receipt for grain.

1. Location and bin number of the grain storage, in which the grain has been deposited.
2. Year, harvest and quality of the grain, deposited.

In Bulgaria the warehouse receipt is issued according to the warehouse register and consists of two parts – collateral and commodity. The ownership of the grain is transferred only with full endorsement of the receipts.

All these features of the warehouse receipt create **the third level of security of the system**. The warehouse receipt bears all the assets of a security and the maintenance of a warehouse register contributes to the additional trust in the system. The important function of the warehouse receipt is determined by the fact that it is the physical carrier of important information, related to the value of the collateral through the precise description of the quality and the quantity of the grain and its right of ownership according to the existent endorsements. The holder of the receipt, according to the grain law is entitled to make claims immediately after the state collectibles and the storage fees owed to the public warehouse and before any other creditors.

NATIONAL GRAIN SERVICE

The National Grain Service is a specialized agency under the Ministry of Agriculture. The National Grain Service is based in Sofia and has regional offices. The major functions of the NGS are as follows:

1. Recommends for licensing the public grain warehouses, organizes and implements control of the licensing process.
2. Keeps and maintains public registers of the public grain warehouses.
3. Executes initial, periodical and special exams of the financial, operational and technical condition of the public grain warehouses as well as the quality and quantity of the stored grain.
4. Collects orders for printing of warehouse receipts.

The operations of the National Grain Service create **a fourth level of security for the system**. The control and the regulation of the performance of the public warehouses and the use of the warehouse receipts aim at a constant level of trust in the system among the users – producers and financial institutions. A secure operation of the public warehouse

provides security for the grain. It is crucial for the users of the system to feel comfortable that the important part of the value of the collateral – its quality and quantity will not be damaged by improper business practice of the public warehouse.

IMPLEMENTATION OF THE WAREHOUSE RECEIPT SYSTEM IN BULGARIA ACCOMPLISHMENTS AND RECOMMENDATIONS

The described legal framework provides an important base for the implementation of the system in Bulgaria. The opinion of the international experts as well as their Bulgarian counterparts, involved in the development of the Grain Law and the regulations attached to it consider the accomplishments so far as very successful and a good start for the practical implementation of the concept and the law into a well functioning system. The next important step is the establishment of the necessary trust in the system among the users – grain producers and processors, grain warehouses and financial institutions.

In order to speed up this process and the system was tested in real conditions in September '98, ACIDI/VOCA with the cooperation of the National Grain Service started a demonstration and educational pilot project. The goal of the pilot project was to test and analyze the advantages and disadvantages of the system in real life Bulgarian conditions and recommend the next appropriate steps for the nation wide implementation.

The methodology of the pilot project included selection of warehouses, producers and banks willing to participate on a voluntary basis. Warehouse inspectors from the USA, teamed with employees of the National Grain Service executed initial and subsequent examination of the participating warehouses. The initial examination determines the financial and technological status of the applicants and the subsequent examination checks the actual quantities of grain described in the financial documents of the warehouse. After the initial exam three warehouses were selected from eight applicants:

- “Zarneni Hrani”JSC – Silistra
- “Kamel” JSC – Kavarna
- “Ustrem” LTD – Rousse

Four production co-operatives and five private producers also participated in the pilot project. Five Bulgarian banks also committed to their participation:

- Central Cooperative Bank
- Hebros Bank
- Express Bank
- Biochim
- Eurobank

The three groups were involved in the negotiation process determining conditions for short term financing based on the use of grain as collateral. The lack of officially used warehouse receipts was substituted by contracts for storage of grain, signed by producer, banker and grain warehouse.

All the participants in the pilot project used access to grain marketing information through the weekly bulletin of the Agency for Agri Market Information (SAPI). This bulletin contained marketing information for domestic and export markets as well as some situation analysis and trends.

As a result of the negotiation process four short-term loans at total amount of 45 000 BGL (about 25 000 USA\$) were given to producers by the regional branches of Hebros bank and Eurobank. The loans were based on 70% of the market value of the grain at the time of signing the contracts.

The pilot project proved that the system could work successfully in Bulgaria and become a vital alternative for short term financing based on the use of grain as collateral. In the course of the pilot project the participants and a team of Bulgarian and American experts evaluated the strengths and the weaknesses of the system at the present stage of development and recommended several important steps for the future implementation. These recommendations are:

- The future development of the grain market in Bulgaria should take a complex approach and include:
 - enforcement of transparent trade rules (regulated and arbitrated by a National Grain Association)
 - create a better access to reliable marketing information
 - upgrade the Bulgarian grain standards to internationally accepted ones
 - develop the organized grain markets (wholesale markets and commodity exchanges)
 - increase the role of the private sector in legislation initiatives and regulation of the market rules
 - optimization of the domestic and export grain market infrastructure

The Pilot Project approach proves to be an extremely important tool for the implementation of a WHR system. It is a comparatively low cost and low risk exercise which from one side tests the different components of the system and identifies potential impediments. A well-designed Pilot Project also has a strong psychological impact on all potential participants and demonstrates to them the advantages of the system.

The next several months after the Pilot Project Evaluation were dedicated to several areas of assistance, which were providing the entire necessary framework for nationwide implementation of the system.

WHR Awareness seminars

Nine seminars have been organized all around Bulgaria in order to make the system popular among as much as possible potential users. The target groups for the seminars were local grain producers, processors, warehouse operators and bankers. The format of the seminars included presentation of the WHR system, sharing experience from American warehouse managers, training in basic principles of grain marketing and presentation of the licensing requirements from the National Grain Service. About 600 people participated in

the seminars and were given opportunity to learn more about the system and express their comments in open discussions.

USA based training for warehouse examiners from the National Grain Service

Two groups of six warehouse examiners from the National Grain Service were sent to the USA on practical training trip. The activity was organized by USDA and funded by USAID. An active partner in design and implementation of the training was the Kansas City Commodity Office. The main goal of the training was to create technical skills in the Bulgarian examiners, by providing them with an opportunity to work with counterpart examiners from the USA. The training was extremely successful and the Bulgarian examiners gained vast experience in initial and subsequent warehouse examination practices.

Assistance to the Ministry of Agriculture in further development of the performance guarantee for the public warehouses.

Two experts from USA worked with the Bulgarian Ministry of Agriculture in developing further the concept of performance guarantee. The first one **Mr. Erwin Schrag** an insurance specialist and former AON executive assessed the insurance market in Bulgaria in order to determine what are the available options for bonding of warehouses or other forms of participation of the insurance companies in the process. His contacts with the private business and government institutions finalized an opinion that bonding is not a very suitable solution for the Bulgarian market for two main reasons: it covers up to 10% of the value of the grain in bonded warehouse and the Bulgarian depositors of grain and creditors require higher level of protection; and second insurance bond is still not a licensed product on the Bulgarian insurance market. Mr. Schrag recommended that the Ministry of Agriculture considers further the establishment of an Indemnity Fund to cover the potential losses of the grain depositors caused by unfaithful performance of the Public Warehouses.

Mrs. Mary McCory, an Indemnity Fund manager from the State of Indiana also visited Bulgaria and provided assistance to the working group in the Ministry of Agriculture, involved in the design of the Bulgarian Indemnity Fund. She advised the working group on the main principles of structuring and managing an indemnity fund and shared a lot of her practical experience from her present job.

Assistance for the Agency for Agricultural marketing information (SAPI)

Dr. William Bailey – Marketing Information Specialist spent two weeks with SAPI, helping them in further improvement of their grain marketing information service. SAPI is building a very good reputation in the country as provider of reliable marketing information covering domestic and international markets.

Licensing process

The National Grain Service started to receive applications for license as Public Grain Warehouse or Grain Storage. Experts from the Service are examining all the application papers and starting initial examination of the warehouses.

On August 3, 1999 the Official Gazette published the Regulation on the Establishment of Indemnity Fund which guarantees the receivables of the depositors and the legitimate holders of warehouse receipts in the public grain warehouses which participate in the indemnity fund. The Fund guarantees the total amount of all receivables of the depositors and legitimates warehouse receipt holders, which derive from the contracts for deposit of grain. According to the above-mentioned regulation each licensed public grain warehouse has to participate in the indemnity fund.

On November 9, 1999, with the approval of the minister of Agriculture, the National Grain Service and three of the licensed public grain warehouses registered an Indemnity Fund “Grain” according to the Regulation on the Establishment of Indemnity Fund (“the Fund”).

The funds for the Fund are raised from:

- Initial payment of the participants (affiliation fee);
- Income from managing the fund;
- Loans;
- Funds received from international projects;
- Other income.

The State Fund for Agriculture approved a three-year loan bearing no interest to the Fund for the amount of 5,000,000 BGL (\$2,500,000). The funds from this loan are part of the capital of the Fund and serve as a guarantee for the receivables of the depositors and legitimate holders of the warehouse receipts.

In October 1999 two other companies received licenses for public warehouses – Roles AD, Varna – grain storage facility in Kardam-Yovkovo with licensed capacity of 8,800 MT and Kaliakra AD, Dobritch – grain storage facility in Dobritch with licensed capacity of 8,000 MT. At the present moment there are 16 licensed public warehouses with total capacity of 192 730 MT.

From Nov. 23rd till Dec. 3rd 1999 ACDI/VOCA organized an East-to-East trip to Hungary and Slovakia for four managers of Bulgarian public warehouses. A representative of the National Grain Service and a representative of ACDI/VOCA joined the group as well.

The study tour program covered visits to licensing institutions of public warehouses in Hungary and Slovakia, public warehouses participating in the warehouse receipts system in Hungary and Slovakia, banks lending money against warehouse receipts as collateral and commodity exchanges in Budapest and Bratislava using warehouse receipts as instruments in grain trade. The participants in the study tour learned about the development of the Warehouse Receipt Systems in Hungary and Slovakia. They also studied the models of cooperation between grain producers, processors and public warehouses.

During the meetings with the banks lending against warehouse receipts the participants gained practical knowledge about all the financial aspects related to using grain

as collateral. They also got acquainted with systems for government supervision and regulation during the meeting with the State Fund for Market Regulations in Slovakia.

At the beginning of December 1999 the public warehouse in Kardam-Yovkovo issued warehouse receipts for 3,800 MT of corn. One producer received financing from Express Bank, Varna by pledging warehouse receipts for 1,800 MT of corn. The bank lent to the corn producer 168,300 BGL (\$89,000). The Dobrich branch of Express Bank lent 187,000 BGL (\$98,000) to another producer from the region who pledged warehouse receipts for 2,000 MT of corn. The bank evaluated the corn of both producers at 170 BGL (\$90) per ton and lent 55 % of its value.

In addition on December 13, 1999 the public warehouse in Popovo issued warehouse receipts for 270 tons of corn to the co-operative in Popovo and the co-operative received 27,540 BGL (\$14,500) loan from Union Bank using the warehouse receipts as a collateral. The bank lent 60 % of the value of the corn. The issue of the warehouse receipts in Popovo and the signing of the Loan Agreement between the co-operative in Popovo and Union Bank were done during a big ceremony which was attended by Minister Ventsislav Varbanov, journalists of 15 national and local newspapers and the national agricultural TV show Brazdi.

ACDI/VOCA together with a Software development company [L@ST](#) LTD created and developed a Web site on Bulgarian agribusiness in November 1999. The web site is active and fully operational. Its goal to be a one-stop shop for agribusiness information of any kind is almost achieved. The site continues to develop and expand its database. On www.bgagro.com agribusinessmen can find necessary information on prices, weather, legislation, industry organizations and more, both in Bulgarian and English.

One very important task for GIDP was compiling of a Warehouse Managers' Operational Manual ("Manual"). At the beginning of October 1999 ACDI/VOCA volunteers – Franklin Ed Gardner and Walter Entgelmeier – visited 3 licensed public warehouses and jointly with the National Grain Service worked on identifying the current problems in warehousing and giving advice for more efficient work. They prepared an outline of the Manual, which was approved by the National Grain Service. A group of Bulgarian consultants in grain storage worked in a team with the National Grain Service and ACDI/VOCA on finishing the Manual. It is a tool on good elevator management practices, giving directions to the warehousemen how to grade, store and handle grain and how to do their book-keeping in accordance with the existing laws and regulations. The Manual was issued in the beginning of June 2000. It is the only complete tool to summarize most of the knowledge and information in this sector of the agribusiness.

In the middle of December 1999 SAPI issued a Bulgarian Grain Industry Handbook both in Bulgarian and English with the financial and technical assistance from ACDI/VOCA. This Handbook provides information about the implementation of the system of licensed public warehouses and warehouse receipts in Bulgaria, the licensed grain storage facilities, the feed and flour mills in Bulgaria and important national and international statistics regarding the domestic and world grain markets.

ACDI/VOCA and USDA together with the National Grain Service and the public warehouse in Targovishte organized a two-day conference in Sandanski. The event was part of the GIDP activities for the implementation of the warehouse receipts in Bulgaria. The major issues were the processes of licensing of public warehouses, warehouse receipts and trade with warehouse receipts, relations among banks, warehousemen and producers, grain handling. ACDI/VOCA and NGS representatives spoke about warehouse receipts, licensing of public warehouses and indemnity fund. Bankers from the first banks that lent against warehouse receipts revealed the opportunities for giving credit to warehousemen and producers. The managers of public warehouses, which issued warehouse receipts and producers, who received them expressed their opinions about the advantages of the system. Donald Graham, ACDI/VOCA American consultant in grain storage and warehouse receipts, presented the warehouse receipts system in the USA. He spoke about grain storage and laboratory equipment too. All the participants (about 150 people attending the event) had the chance to express their attitude to the problems in the discussion panels. The conference gathered warehousemen, bankers, grain producers and dealers and government officials to discuss the important issues of the grain business.

All the components of the system were in place in harvest 2000. Many grain producers and processors used the warehouse receipts system in the summer and fall of the year. More than 200 000 MT of grain was deposited in the public warehouses and over 320 receipts were issued. As of December 2000 the deposited volumes are more than 100 000 MT. SG Expressbank, Union Bank and United Bulgarian Bank gave credit to depositors against warehouse receipts alone. Several months after harvest the 3 banks together lent about \$US 3 500 000 (BGN 7 800 000) to receipts holders, thus allowing them to cover for their current expenses without selling the grain right at harvest (the price at that time was 170-180 BGN/MT, VAT excluded). Seven months after harvest the grain price was 240-250 BGN/MT (VAT excluded). The additional generated profit (loan and storage expenses included) for the receipts holders was 40-50 BGN/MT, which makes it 30% more than the one at harvest time. In the meantime the grain was stored in the secure licensed public warehouses, and the depositors received credit collateralized by warehouse receipts only.

The warehouse receipt system is developing steadily and intensively. In November 2000 ACDI/VOCA organized an US-based training for the managers of 6 public warehouses. During the trip they learnt about the specifics of the American warehouse receipt system, grain growing technologies in US and the work of the federal and state institutions in the grain sector. They also visited typical US farms and licensed public warehouses. In terms of grain marketing, the Bulgarian warehouse managers visited the Kansas City Commodity Exchange, as well as the federal laboratory that exerts control over the grain grading.

ACDI/VOCA together with the National Grain Service will continue to organize awareness seminars and workshops for the public warehouses and grain storage facilities, grain producers and processors, bankers and representatives of the Ministry of Agriculture and the NGS for further expanding the warehouse receipt system in Bulgaria. ACDI/VOCA and NGS organized a panel of awareness seminars in the regions of the newly licensed public warehouses in February 2001. More meetings are to be organized in the months before harvest to prepare the producers how to use the warehouse receipt system. The efforts in this direction are very important since bringing knowledge to the basic users of the system is key for its successful implementation.

ACDI/VOCA, USDA and NGS organized a National conference on the licensing and control of the public warehouses and grain storage facilities and evaluation of the warehouse receipt system implementation in 2000. The conference took place on March 5-6, 2001 in Albena. Representatives of the public warehouses and grain storage facilities, state officials, banks, grain producers and others were present. 2 federal USDA warehouse examiners attended the event – Kenneth Beck and Franklin Ed Gardner. The general attitude towards the current status and future development of the system was positive. All the participants agreed that all the components of the system are in place and the further needed support is in the area of spreading more information and making it popular among the users of the system.

LICENSING PROCESS IN BULGARIA:

As of March 1, 2001:

- I. Licensed grain storage facilities – 114; total capacity – 815 000 MT
- II. Licensed public grain warehouses – 23; total capacity – 252 595 MT
 - 1. Zarnoizkupuvane (Targovishte) - 20 000 MT
 - 2. Zarneni hrani (Silistra) - 30 000 MT
 - 3. Kristera (Popovo) - 41 930 MT
 - 4. Roles (Kardam - Jovkovo) - 16 000 MT
 - 5. Kaliakra, Dobrich - 8 000 MT
 - 6. Fortuna 3000 (Biala Slatina) - 3 000 MT
 - 7. Papas Oil - Blachik - 5 000 MT
 - 8. Papas Oil - Tenevo (Iambol) - 10 000 MT
 - 9. Parvi mai (Silistra) - 5 000 MT
 - 10. Zarnobaza (Spasovo) - 3 000 MT
 - 11. Melinvest (Isperih) 10 000 MT
 - 12. Melinvest (Radnevo) 5 000 MT
 - 13. Zarnobaza (Shabla) 15 000 MT
 - 14. Zarneni Hrani Silistra (Alfatar) 10 000 MT
 - 15. Zarneni Hrani Silistra (Tutrakan) 10 000 MT
 - 16. Zlatev Zarno (Varna) 3 665 MT
 - 17. Zlatna Trakia (Biala) 10 000 MT
 - 18. Zarneni Hrani (Balchik) 20 000 MT
 - 19. Ptitzeklannitza (Dobrich) 3 000 MT
 - 20. Agroluks (Varna) 6 000 MT
 - 21. Prolet (Knezha) 5 630 MT (the license is withdrawn)
 - 22. Niva (Kostinbrod) 4 000 MT
 - 23. Protein, Shumen (Veliki Preslav) 5 000 MT
 - 24. Zarneni Hrani Silistra (Varna) 9 000 MT

TOTAL CAPACITY: 252 595 MT

LESSONS LEARNED

After one year of countrywide implementation of the WHR system in Bulgaria the project management feels comfortable of making the following conclusions, which may contribute, for the creation of an implementation model, that can be used in other countries.

I. Main barriers and impediments for the implementation of the program and solutions to them :

A. **Technical:** The WHR implementation program did not face substantial technical problems due to the available USAID funding and ability to mobilize the best expertise and technical knowledge. The program had an access to extremely qualified consultants and volunteers, who did their best in identifying the optimal solutions for the Bulgarian environment. The availability of the highly professional expertise of USDA employees involved in creating the enabling legislation and control of the system, together with the strong support of the private grain sector and finance professionals contributed greatly to the proper implementation strategies.

B. **Institutional:** The implementation process has been supported by all key institutions along all phases. The international donors and USG organizations coordinated their effort of support and provided a broad platform for development of all the necessary components. USAID as the major sponsor of the project made sure all necessary resources are available for ACDI/VOCA for the proper implementation process. EBRD contributed an extremely valuable input in the development of the secondary legislation in such a way that the financial institutions feel comfortable with using the WHR instrument. The World Bank included the development of WHR system in Bulgaria as a major requirement for the negotiation process for two big loans to the government of Bulgaria. Throughout the whole process, ACDI/VOCA received the full support of The Ministry of Agriculture and The Agricultural Commission in the Parliament.

From institutional standpoint the biggest challenge for the program was to create trust in the system among the participants and mainly the grain producers and the banks. The history of government owned grain storage facilities which were in monopolistic situation and several cases of newly privatized elevators who applied unfair business practices, created a high level of unwillingness of the producers to use third party services for grain storage. It took long educational efforts and face to face meetings with the licensed warehouse operators before the two parties got into business. The financial sector in general is skeptical towards agricultural lending, because of the inherited higher risk in the system. The program implementers spent a lot of efforts working with the banks and taking in considerations all their concerns in order to end up with legislation and systems of control and financial guarantees, that would be acceptable.

C. **Legal:** One of the advantages of the implementation approach in Bulgaria was the availability of several legislative models, which served as a reference point through all the steps in the development of the proper legislation. Most of the basic features of the Bulgarian Grain Law are after the Grain Warehousing law in

the USA. The Bulgarian legislators were also able to get useful tips from the Hungarian and Slovakian laws that regulate WHR systems in these countries.

The historical existence of a similar legislation before World War II in Bulgaria, was an additional advantage from the stand point of the ability of the legal consultants to take ideas about approaches that already proved their efficiency in the local conditions.

One of the legal impediments was that The Commercial Code of Bulgaria has a section on the general principles of warehousing services for all types of commodities, without taking in consideration the specific technicalities of grain warehousing operations. In some articles of the Grain Law there are straight referrals to the Commercial code, which need to be further clarified and is a matter of amendments and improvement of the existing Grain Law. For example the Commercial Code imposes some limitations for the warehouse operator to pledge goods through warehouse receipts, which are his own property. The Grain Law does not prohibit the public warehouse operators to issue receipts for their own grain, but the use of this feature of the WHR system in real life needs some further improvement of the way the two laws correspond.

Another important legal barrier is the inability of the indemnity fund to get an active participation in the procedures in case of bankruptcy a warehouse. The indemnity funds management in USA poses the authority of executing all the procedures related to handling a situation of financial default or felony from a public warehouse. They are able to react fast, take control of managing the assets and goods of the warehouse and start procedure of liquidation of the company and satisfaction of the demands of the depositors and creditors. In Bulgaria, all this actions are within the competence only of the court. The recommendations for future improvement of the legal framework will put a serious emphasis on this issue.

A very important barrier from the standpoint of the financial institutions comes again from provisions in the Commercial act, which put the state and the warehouse, before the creditor in a procedure of claims. Some of the banks with the assistance of legal advisors managed to resolve this problem, by requesting the formation of a special pledge on the grain. A separate law regulates the special pledges. All special pledges are entered in a central register and in that case the creditor becomes the first one to execute claim against the borrower.

II. Improvement of the accessibility of small operators and farmers to the system

The limitations for access to the WHR system in Bulgaria are practically only for the warehouses. The licensing requirement for financial ability and technical capacity are necessary for the warehouses to be able to perform their major obligation – to guarantee the quantity and quality of the grain as it is described on the warehouse receipt. Obviously these minimum requirements will vary in different countries, so a proper expertise should be in place in each case to determine what are the optimal ranges. The WHR system does not discriminate among the depositors, which are able to use it. The grain is stored commingled in the warehouses, unless the depositor especially wants them stored separately and is ready to cover the costs. In that case there are no limitations for the volumes

stored under warehouse receipts and small farmers are able to use the system in the same way as medium and large ones.

There are several incentives, which could be used to make the access of small farmers to the system easier. One of them is a government program for subsidizing the storage fees in public warehouses. This approach has been used in Bulgaria as a short-term incentive for support of the WHR system. The State Fund Agriculture, provided storage subsidies for producers, used public warehouses after harvest 2000. This measure proved to be extremely popular and increased the participation of the small producers in the system.

Another possibility is for the commercial banks that lend against WHR to lower their interest rates for this type of loans. The banks should be able to do so based on the higher liquidity of the collateral they receive and the additional levels of protection of the system.

III. Key components for the successful implementation of the system :

The body of the present report describes in details all the key components that are necessary for the implementation of the WHR system. At this point I would like to provide a summary of all priority components that each implementation approach should take in consideration.

- A. Consensus between the government authorities, the financial sector and the private industry about the necessity and the advantages of implementing WHR system. Without this common platform the development process could be very difficult. We have observed cases where because of lack of political will, the development of a proper legislation was slowed down and although all the rest of the participants were ready to get in the process, results were delayed. Here I would like to especially outline the role of the government institutions in the implementation process. The development of a proper legislation requires a full support of the legislators and government officials. They should be open to discussion with the private sector and the international experts on the best legal approaches for the specific country environment. The formation and management of the regulatory agency is a key component for the functioning of the system. Government institutions could play an important role also in introduction of incentives that would support the initial stage of development of the system
- B. Involvement of at least one of the big international donors, committing resources for development of the system. Starting from scratches in developing a very complex approach which involves creating legislation, systems of financial guarantees, regulatory agency and private sector awareness is a time and resource consuming effort. The implementing agent should be able to get access to the best expertise available and make sure all the components of the system are developed in parallel. The unique combination in Bulgaria having all the donors on the same agenda (USAID, USDA, The World Bank, and EBRD) was a favorable condition that contributed for the overall implementation process.

- C. Involvement of an experienced implementing agent is an important component of the overall success. The agent should have the appropriate implementation know how and access to the required expertise and resources.
- D. Comprehensive feasibility study of the country specific potential for development of the system. This assessment would be also a good basis for implementation methodology
- E. Development of country specific implementation plan that very clearly defines the methodology and sequence of activities as well as the package of implementation tools that are appropriate for achieving the final goal.

The successful WHR system implementation in Bulgaria as well as several other examples of viable commodity linked systems for finance in countries like Hungary, Slovak Republic and Russia create a definite belief that this type of solutions for markets facing difficulties with loans collateralization are viable tool for access of small and medium size producers to finance. The WHR systems play extremely important role for the general development of marketing infrastructure and contribute to increasing the added value of the agricultural sector. The recent interest in this type of systems in countries like Kazakstan, Romania, Turkey and Croatia demonstrates the future potential and challenge for the development effort.