

RURAL LENDING – WARRANTS CERTIFICATE LEGISLATION

Technical Anchor (TAN) TERMS OF REFERENCE

Project Owner: Radu Negrea (RBA)

Project Manager: Marilena Popovici (Bancpost)

Deputy Project Manager: Aurica Stoica (Ministry of Agriculture, Forests and Rural Development)

Project Working Group: Rural Credit Guarantee Fund (1 expert), NBR (1 expert)

Project Objective:

To provide the Project Working Group (PWG) with a thorough analysis of how bank rural lending (products, policies, processes, procedures and target clients) is done under the current regulation and how it is likely to benefit from the new regulatory solutions under consideration.

Role:

It is expected that TAN will perform the following functions, also drawing from the PWG TOR (attached):

During the project:

- With the support of PM/DPM/SPI Secretariat, TAN will assess how bank rural lending business is run under current regulations and how it could evolve under a more robust regulatory framework, specifically in terms of warrant certificates;
- Ramona Bratu of the SPI Secretariat will provide TAN with support for his preparatory and background work as well as during his field work;
- TAN will interact with and provide expert advice to PWG while the latter is in the process of preparing specific regulatory recommendations to ensure they meet business needs.

Project advocacy:

- At the completion of his field work task, TAN will present the PWG his findings.

Back to office report

- A calendar week after the PWG presentation, TAN will deliver final document (taking into account PWG discussion of his findings)

Reporting:

Operational: Project Manager
Administrative: Ramona Bratu.

Estimated Number of Days:

TAN's assignment is expected to take up to 2 weeks of field work in Bucharest/rural areas (15 working days including preparation and report writing time, week-end work and travel time).

Output:

A report that will describe a) current rural lending practices, focusing on products, processes, risk mitigating measures, clients, volumes; b) business relevance of suggested strengthening of regulatory framework (e.g., warrant certificate regulations); and c) changes in bank products and procedures that will be necessary to maximize impact from new legislation. Draft report to be presented before the PWG and to be finalized by one calendar week later.

PROJECT TERMS OF REFERENCE

Project: Rural Lending (Warrants – deposit certificates)
Project Owner: Radu Negrea (on behalf of RBA)
Project Manager: Marilena Popovici (Bancpost)
**Deputy Project Manager: Aurica Stoica (Ministry of Agriculture,
Forests and Rural Development)**
Technical Anchor: TBD

I- Background

In Romania, agricultural lending represents a modest share of total bank loans, estimated in July 2004 at a mere 2.6% of the total bank loans above EUR 5,000 that were extended. The high transaction costs and risks are the main factors that affect the supply of credit in rural areas. One of the drawbacks perceived by banks in rural financing is lack of clarity of the legislation regulating the use of the ownership title (warrants-deposit certificates) for agricultural products.

Initially regulated by a law from 1937, the regime of warrants - deposit certificates for crop inventories was further clarified between 2000 and 2003 in six legislative acts (Government Emergency Ordinance no. 56/2000 approved and modified by Law no. 39/2001; Government Emergency Ordinance no. 109/2000 approved by Law no. 657/2001; and Government Emergency Ordinance no. 141/2002 approved by Law no. 39/2003) and some additional methodological norms. The main provisions of the regulatory framework are:

- the deposit certificates for crop inventories represent bearer negotiable titles, issued by depositaries in exchange of crop inventories deposited in the warehouses;
- in order to issue deposit certificates, the depositaries have to be inspected and licensed by the Ministry of Agriculture, Forests and Rural Development or an authorized inspector, based on a verification of the depositary's compliance with the requirements for storing crop inventories;
- the Deposit Certificates Guarantee Fund (DCGF) is established as a public institution, in order to guarantee the reimbursement of the crop inventories value as stated in the deposit certificates. The depositaries that have been licensed have to open a deposit in the account of the DCGF in an amount representing 0.5% of the market value of the stored crop inventories for which have been issued deposit certificates. The organization and functioning of the DCGF are established by its by-law, approved by the Government following a proposal of the Ministry of Agriculture, Forests and Rural Development.

So far, the implementation of the regulatory framework yielded poor results. DCGF has only been established on paper and no deposit certificates for crop inventories have been

issued. Also, according to some authorized sources, only one depository has been licensed to issue deposit certificates.

According to other countries' experience, lending against warrants-deposit certificates on cereals has the potential to increase commercial banks' lending to agriculture, by reducing the credit risk, lowering transaction costs, and improving loan recovery. The value of cereals that are warehoused in one year (about EUR 900 million) can give an indication of the potential of rural lending based on warrants – deposit certificates.

II - Project Objective

To prepare a set of specific recommendations (“secondary” rules and regulations and technical and organizational implementation steps) on the measures needed to be undertaken by the competent authorities, market participants and other institutions in order to remove the existing roadblocks to the development of the agricultural warrants-backed lending within acceptable risk parameters.

III – Intended Strategy

The project management group (Project Owner, Project Manager, Deputy Project Manager, supported by the SPI Secretariat) acts based on the mandate received from the SPI Committee to prepare a set recommendations on the measures needed in order to remove the existing roadblocks to the development of the agricultural warrants-backed lending, including proposals for “secondary” rules and regulations, supported by a RIA of the proposed regulatory changes.

The project management group (PMG) should gain a satisfactory understanding on the drawbacks perceived by various stakeholders in the application of the current legislation. The SPI Secretariat will provide a compilation of the existing legislation on the matter.

PMG should hold preliminary meetings with representatives of the relevant organizations in order to get their views on the issues raised by the current legislation, as follows:

- Organization of the Commercial Depositories from Romania (Organizatia Depozitarilor Comercianti din Romania, ODCR): to acquire an understanding of incentives, costs and risks for obtaining the license to issue deposit certificates for crop inventories;
- Ministry of Agriculture: to acquire an understanding of the perceived impediments on establishing the DCGF and the licensing process of depositories.

Likewise, PMG will meet with representatives of the banking industry and regulators in order to understand the implications and the risks of developing of a warrants-backed rural lending market:

- rural areas regional bank managers: to outline the characteristics and risks of rural lending;
- RBA: to provide insights on the issues outlined in the discussions on the matter held so far within the RBA Technical Commissions;

- PWG members from banks: to provide a perspective on the potential for increasing the lending to agriculture based on warrants – deposits certificates, outlining the specificities of the lending process and procedures for this new business and the perceived risks and costs;
- NBR: to provide a supervisory perspective on the ways in which agricultural lending backed by warrants – deposits certificates could be kept within acceptable risk parameters.

In order to outline the possible solutions, PM/DPM/SPI Secretariat will ask:

- Rural Credit Guarantee Fund: to share its experience in terms of operating procedures and present its point of view on how the process of establishing the DCGF could be facilitated;
- Ministry of Agriculture: to conceive a possible system of incentives for the depositaries to apply for licenses (improving the process of solving the requests from depositaries and other possible legal and practical stimulants).

Based on the information gathered as described above, the SPI Secretariat will prepare an issues paper for PWG discussion.

The project working group (PWG) will analyze the drawbacks perceived by various stakeholders in the application of the current legislation and will outline possible solutions to mitigate them, incorporating safety measures to ease the risk concerns of banking sector and regulators. These aspects will be outlined into an interim report.

Following the discussion of the interim report, the PWG will draw up a set of specific recommendations on the “secondary” rules and regulations and other organizational improvements needed to remove the existing roadblocks to the development of the agricultural warrants-backed lending, supported by a RIA of the proposed regulatory changes and benchmarking with existing international practices as provided by the SPI Secretariat. Likewise, the PWG will indicate the main technical implementation steps required by the proposed “secondary” rules and regulations.

PM/DPM/SPI Secretariat will consult with relevant stakeholders on the feasibility of the proposed specific recommendations prepared by the PWG before finalizing the SPI Committee Actionable Report.

IV- Methodology: from kick off to the accomplishment of the project

Preparation of PWG 1st meeting (PM/DPM and SPI Secretariat) - January 25 – February 16

The project management group (PMG) will build a common understanding on the drawbacks perceived by various stakeholders in the application of the current legislation. The SPI Secretariat will prepare a compilation of the existing legislation on the matter. The PMG/SPI Secretariat will have preliminary meetings with the Organization of the Commercial Depositaries from Romania (to understand the incentives, costs and risks for

obtaining the license to issue deposit certificates for crop inventories), with the Ministry of Agriculture (to acquire an understanding of the perceived impediments on establishing the DCGF and the licensing process of depositaries), and with rural areas regional bank managers to discuss characteristics and risks of rural lending. PM/DPM/SPI Secretariat will also ask the RBA to provide insights on the issues outlined in the discussions on the matter held so far within the RBA Technical Commissions.

PO/PM will send to the PWG members the SPI Committee Mandate Letter together with the following documents before the PWG 1st meeting:

1. An issues paper prepared by the SPI Secretariat, based on the following information:
 - a. the results of the interviews with the Organization of the Commercial Depositaries from Romania, the Ministry of Agriculture, the rural areas regional bank managers and the discussion with the RBA;
 - b. Ministry of Agriculture: an overview on how it solves the requests received for licensing the depositaries to issue deposit certificates for crop inventories in the application of the law (outlining procedures for solving requests, number of requests received, number of requests solved, length of solving the requests and practical problems encountered in the application of the current legislation) and a proposal on (i) how the process of establishing the DCGF could be speed up and (ii) a possible system of incentives for the depositaries to apply for licenses (improving the process of solving the requests from depositaries and other feasible legal and practical incentives);
 - c. Banks: a perspective on the potential for increasing the lending to agriculture based on warrants – deposits certificates, outlining the specificities of the lending process and procedures for this new business and the perceived risks and costs;
 - d. NBR: a supervisory perspective on the ways in which agricultural lending backed by warrants – deposits certificates could be kept within acceptable risk parameters;
 - e. Rural Credit Guarantee Fund: a document outlining its experience in terms of operating procedures and presenting its point of view on how the process of establishing the DCGF could be facilitated.
2. Draft TORs prepared by SPI Secretariat and endorsed by PO and PM/DPM.

PWG 1st meeting - February 19 - 23

1. PWG members discuss the issues paper prepared by the SPI Secretariat;
2. PWG members take stock of the drawbacks perceived by various stakeholders in the application of the current legislation;
3. PWG members outline possible solutions to overcome the difficulties perceived by various stakeholders in the application of the current legislation;
4. PWG members agree on a list of issues that can be addressed by issuing “secondary” rules and regulations;
5. PWG member from the Ministry of Public Finance provides an opinion on the proposed regulatory changes;

6. PWG members prepare an outline of an interim report to include an analysis of the drawbacks perceived by various stakeholders in the application of the current legislation and outline possible solutions to mitigate them, incorporating safety measures to ease the risk concerns of banking sector and regulators;

4. PWG members agree on TORs prepared by SPI Secretariat and endorsed by PO and PM/DPM;

5. PM/DPM establish **homework** for PWG members:

PM/DPM/SPI Secretariat: prepare the interim report;

SPI Secretariat: prepare a draft questionnaire for gathering needed data for RIA, based on the information on costs and risks received from the PWG members, to be discussed at the PWG 2nd meeting and prepare a compilation of relevant international laws;

Each PWG member: prepare position documents on the technical and organizational implementation steps needed to efficiently enforce the proposed “secondary” rules and regulations.

The individual contributions will be sent to the PM/DPM and SPI Secretariat. SPI Secretariat will prepare a centralized document on the technical and organizational implementation steps needed to efficiently enforce the proposed “secondary” rules and regulations to be circulated before the PWG 2nd meeting, together with the compilation of relevant international laws.

PWG 2nd meeting - March (12-16)

1. PWG members take note of the interim report and discuss any suggestions received;
2. PWG members take note of existing relevant international practices;
3. PWG members agree on a specific set of recommendations on the “secondary” rules and regulations needed to remove the existing roadblocks to the development of the agricultural warrants-backed lending, in line with existing international practices;
4. PWG members will agree on the technical and organizational implementation steps needed to efficiently enforce the proposed “secondary” rules and regulations;
5. PWG members prepare an outline of a common position paper to include the recommendations on secondary regulations to be issued and technical and organizational implementation steps needed to remove the existing roadblocks to the development of the agricultural warrants-backed lending within acceptable risk parameters.
6. PWG members approve the RIA questionnaire;
7. PM/DPM establish **homework** for PWG members:
 - PWG members: prepare specific sections of the common position paper as indicated by the PM/DPM;
 - PM/DPM/SPI Secretariat: finalize the position paper to support the proposed recommendations based on consultations with relevant stakeholders on the proposed specific recommendations.

PWG 3rd meeting - March (26-30)

1. PWG members discuss and approve the final position paper;
2. PWG members validate RIA findings;

Homework: SPI Secretariat: integrate the RIA findings into the final document to be presented for SPI Committee endorsement.

V- Output

PWG 1st meeting

- PWG members send individual contributions;
- PWG members agree on a list of issues;
- PWG members agree on possible solutions;
- PM/DPM/ SPI Secretariat prepare report.

PWG 2nd meeting

- PWG members approve the RIA questionnaire;
- PWG members agree on specific recommendations on the “secondary” rules;
- PWG members agree on technical and organizational implementation steps;
- PM/DPM/SPI Secretariat prepare position paper.

PWG 3rd meeting

- PWG members approve position paper;
- PWG members validate RIA findings;
- SPI Secretariat sends SPI Committee Actionable Paper to Convergence.

VI - Project Team

The team will be composed of:

- Ministry of Agriculture
 - 1 expert with experience in applying the legislation on warrants – deposit certificates;
- Rural Credit Guarantee Fund
 - 1 expert;
- Banks
 - 2 experts from banks from the Lending Departments of banks with large territorial networks in rural areas, of which one from the RBA Bank Lending Commission;
- National Bank of Romania
 - 1 expert from Supervision Department with credit risk background;

- Ministry of Public Finance
 - 1 expert from the General Department for Legislative Harmonization and European Integration.

The team will be chaired by the Project Manager and co-chaired by the Deputy Project Manager.

PM/DPM have to report to PO at least after each meeting of the PWG.