

Negotiability of the Warehouse Receipt in the Context of Banking Reforms

DR.SUBHASH C BATRA AND PROF. M S TURAN

A number of commissions and committees were appointed by the Govt. of India from time to time for finding ways to reduce rural indebtedness. It was only after the All India Rural Credit Survey Committee had reiterated in 1954, the need for providing warehousing in the public sector, that the concept of public warehousing took a concrete shape. The term "Warehouse Receipt" has been defined in the State Warehouses Acts which regulate the activities and running of public warehouses in the respective state. There has been no legal binding on Banking Institutions to accept the Warehouse Receipt as a collateral security. The Reserve Bank of India has been issuing directives from time to time about the advances against the pledge of the stocks covered by the Warehouse Receipts. The Government of India having seized of the issue, has recently brought out a Central Legislation for making the Warehouse Receipt a fully negotiable instrument.

INTRODUCTION

Even though tremendous progress has been achieved in different sectors of the economy over the years since independence, yet India continues to be recognized as an agrarian economy even today and that Agriculture Sector occupies a pivotal position in India's economy. Reforms in any sector are a perpetual proposition. Reforms today have become more focused in view of the fast changes taking place the world over due to tremendous technological advancements and emergence of rapid globalization process. Imperatively, banking reforms would thus become meaningless, if these are not Agricultural focused. As a matter of fact the need for licensed public warehouses had primarily been felt in the context of the policy of extension of agricultural credit to rural areas.

The "Warehouse Receipt" which evidences a contract for storage and is issued by a licensed warehouse in the prescribed form to a person depositing goods in the warehouse, is usable for the creation of credit facilities by the

Dr.Subhash C Batra, Secretary, Central Warehousing Corporation; Y-15, Hudco Place, Andresgunj, New Delhi-110 049.

Prof. M S Turan, Formerly Professor in the Haryana School of Business, G.J.University of Science and Technology, Hisar (Haryana)-India.

commercial banks and other financial institutions to the agriculturists, farmers and traders. The commercial banks and other financial institutions accept the Warehouse Receipt as a collateral security and advance loans against it. It has a vast potential for the commercial banks and other financial institutions to provide finance to the agriculturists both the producers and the dealers. A fully negotiable Warehouse Receipt backed with the essential ingredients of fiduciary trust and the description mentioned thereon of the goods based on proper scientific analysis have an immense potential of revolutionizing the commodity markets and thereby proving to be an important tool. It would, therefore, be timely that we discuss about the negotiability of the Warehouse Receipt while deliberating on and considering the banking reforms in the country.

HISTORICAL BACKGROUND

In India, the concept of public warehousing took shape mainly because of widespread rural indebtedness. The Indian economy, being agro based had been experiencing the exploitation of farmers by middlemen due to widespread and growing rural indebtedness. It was felt that overwhelming majority of the farmers were heavily indebted primarily because they were forced to sell their produce immediately after the harvest at very low prices just to repay the loan obtained before harvest or to pay the loan and interest running outstanding generation to generation. This coupled with excessive pressure of growing population and its dependence on agriculture had resulted into smaller holdings of land which were proved uneconomic, leading to a vicious cycle of rural indebtedness. The exploitation of farmers by middlemen and growing rural indebtedness in India coupled with distress sale of agricultural produce by farmers and lack of regulated agricultural marketing had attracted the attention of Government of India as far back as 1928 when the Royal Commission on Agriculture while pointing out serious deficiencies in agricultural marketing due to non-availability of storage facilities had first recommended for the establishment of licensed warehouses. Several exercises were thereafter conducted by a number of Commissions and Committees particularly the Agricultural Finance Sub-Committee under the Chairmanship of Prof. D.R.Gadgil (1945), the Rural Banking Enquiry Committee ((1950) and All India Rural Credit Survey Committee (1954) appointed by the Reserve bank of India for finding ways to reduce rural indebtedness. These Commissions and Committees went into various aspects of this problem and pointed out the imperative need for public warehousing in the organized sector to regulate agricultural marketing and to reduce the burden of rural indebtedness. The Rural Banking Enquiry Committee (1950) had emphasized the importance

of storage and warehousing in relation to rural credit and rural banking. These Commissions and Committees had observed lack of credit facilities to the agriculturists and felt that the volume of finance supplied by the commercial banks to the agriculturists could be considerably increased by improving the arrangements for marketing of crops by grading and standardization, creation of proper storage facilities and ushering in regulated markets. They had also felt that the establishment of warehouses in which the goods could be stored against a negotiable receipt usable for obtaining loans from banks be introduced in India. The All India Rural Credit Survey Committee (1954) in its report had stressed the need for establishing licensed warehouses scientifically managed as per prescribed standards with specific objective of developing warehouse receipt a negotiable paper which could constitute a first class security and open out important avenues to the commercial banks to provide finance to the agriculturists – both the producers and the dealers. The construction of warehouses was unlikely to attract sufficient private capital immediately. It was also not considered desirable to leave the running of warehousing system in private hands and thus the States were asked to take it up as an extension of the transport system. Various efforts made in this regard by the Reserve Bank of India did not turn into reality. The All India Rural Credit Survey Committee had observed that the most important reason for this lack of progress, in spite of a large mass of legislation in regard to warehousing, had been the fact that no specific body or institution had displayed real interest in storage and warehousing. The Committee had also referred to other grave difficulties as were connected with the grading of agricultural commodities, the availability of adequate personnel, and the question of providing training facilities for such personnel and so on. The Committee had also recalled what the Agricultural Finance Sub-Committee had said in 1945 that the construction of a chain of warehouses was unlikely to attract immediately sufficient private capital and it might also not be desirable to leave the running of the warehousing system in private hands and had thus recommended that the State should itself undertake, as part of its programme of development of rural transport, the planning and construction of warehouses at all nuclear points of trade in agricultural produce and the warehouse system should be operated by a public corporation in order to also facilitate the “issue of warehouse bills.”

It was, therefore, only after the All India Rural Credit Survey Committee had reiterated in 1954, the need for providing warehousing in the public sector, that the concept of public warehousing took a concrete shape.

Based on the recommendations of the All India Rural Credit Survey

Committee, the Parliament passed the Act called 'The Agricultural Produce (Development & Warehousing) Corporations Act, 1956. In this Act, the recommendations made by the aforesaid Committee were broadly incorporated. The Act of 1956 was, however, later on repealed and replaced by another Act known as "Warehousing Corporations Act, 1962". The reason for this change was that it was felt that the two functions viz. (i) the development of cooperative economic activity, marketing, processing and (ii) the development of Storage, Warehousing and distribution assigned to the National Cooperative Board should be bifurcated and kept under separate statutory organizations and that it was not necessary to continue the Central Warehousing Corporation under the control of the Board. Along with the Central Warehousing Corporation, State Warehousing Corporations in some of the States were thus set up under this Act. One of the main objectives of these warehousing Corporations has been the Creation of a negotiable paper to provide as an instrument for expansion of credit through commercial banks for the benefit of producers, dealers and others.

THE TERM "WAREHOUSE RECEIPT" AND ITS NEGOTIABILITY

The term "Warehouse Receipt" has been defined in the State Warehouses Acts which regulate the activities and running of public warehouses in the respective state. "Receipt" means a Warehouse Receipt in the prescribed form issued by a warehouseman to a person depositing goods in the warehouse. A Warehouse Receipt thus contains full particulars of the depositor, commodity, its grade and value. The terms and conditions on which goods are accepted for storage and which are framed on the basis of various provisions of the State Warehouses Acts and rules made there under are also prescribed on the Warehouse receipt. A licensed warehouseman under these Acts is authorized to issue a negotiable or a non-negotiable Warehouse Receipt.

As per Section 13 of the Negotiable Instruments Act, 1881, a negotiable instrument means a Promissory Note, Bill of Exchange or Cheque payable either to order or to bearer. The Negotiable Instruments act, 1881, thus, does not define the characteristics of a document to be a negotiable instrument. However, the essential feature of a negotiable instrument is its negotiability. The Warehouse Receipt is not listed as a negotiable instrument in the Negotiable Instruments Acts, 1881. However, Section 2(4) of the Sales of Goods Act, 1930 brings it within the ambit of the definition of a document of title. Further it evidences a contract for storage of goods under the Indian Contract Act, 1872.

The provisions in the State Warehouses Acts passed by the various State governments provide that unless otherwise specified in the Warehouse

Receipt, a receipt issued by a warehouseman is transferable by endorsement and entitles its lawful holder to receive the goods specified in it on the same terms and conditions on which the person who originally deposited the goods would have been entitled to receive them.

The transfer of Warehouse Receipt from one person to another means transfer of the right to receive the delivery of the goods covered by that Warehouse receipt. The banking institutions accept the Warehouse Receipt as a collateral security for advancing loans and become the holder in due course of the Warehouse Receipt. It is the liability of the Warehouseman to return on demand or surrender of the Warehouse Receipt, the goods of the same quality and quantity (subject to natural loss in storage due to shrinkage etc.) which were tendered for storage by the depositors. The Warehouse Receipt has the same features as in case of Promissory Note except for the difference that the former deals with the goods and later with money.

MAJOR CONSTRAINTS IN MAKING WAREHOUSE RECEIPT A FULLY NEGOTIABLE INSTRUMENT

Despite various provisions relating to the negotiability of the Warehouse Receipt as discussed above, nevertheless, even after a period of five decades, the position is that the usage of Warehouse Receipt has remained restricted to be accepted by the Commercial Banks as a collateral security for grant of loans against the goods stored in the warehouses and the Warehouse Receipt has not yet gained its acceptability as a negotiable instrument that it could be freely transferred from one person to another. The Warehouse Receipt at the present cannot be brought under the purview of the Negotiable Instruments Act, 1881 which deals only with the monetary transactions through the specified instruments such as Promissory Notes, Bill of Exchange and Cheques. The Reserve Bank of India has already expressed that it is not feasible to include the Warehouse Receipt as a negotiable instrument in the Negotiable Instruments Act, 1881 and have thus recommended for bringing a separate central legislation for making the Warehouse Receipt a fully negotiable instrument.

Over the period, due to changes in the economic policies of the country particularly the nationalization of the business of food grains during the year 1964 and introduction of Minimum Support Prices and the procurement of the food grains by the Govt. of India through state procurement agencies, almost negligible storage surpluses were left with the agriculturists and others and thereby rendering no effective attention about the serious implementation of the legislative framework provided for making the Warehouse Receipt a negotiable instrument and that the Warehouse Receipt could get general acceptability to be regarded as a negotiable instrument.

There has been no legal binding on Banking Institutions to accept the Warehouse Receipt as a collateral security. The Reserve Bank of India has been issuing directives from time to time about the advances against the pledge of the stocks covered by the Warehouse Receipts. In the past, as a result of curbs imposed by the Reserve Bank of India, there has been a decline in the advances against the Warehouse Receipts. The free flow of credit against the Warehouse Receipt from the Banks to the depositors has not been possible due to various restrictions imposed by the Reserve Bank of India under the credit control schemes.

The legislative framework under the State Warehouses Acts enacted by various State Governments provided for the "lawful holder" to receive the goods in the event of transfer of the Warehouse Receipt from one person to another, thereby putting the onus on the holder of the Warehouse Receipt to prove that he was the lawful or bonafide owner of the goods covered by the Warehouse Receipt. This, therefore, restricted the easy transferability of the Warehouse receipts. The legislative framework for the negotiability or transferability of the Warehouse Receipts being under the respective State Acts, it envisaged jurisdictional problems and restricted the negotiability of the Warehouse Receipts to other geographical locations falling in other States. The Banking Institutions have, therefore, been declining the loans and advances to the second and subsequent holder of the Warehouse Receipt.

Various official policies nevertheless discourage the use of Warehouse Receipts, particularly the very high level of public intervention in the market for food grains and sugar and sales taxes which tend to drive trade into informal channels. Dynamic tariffs on imports, storage control orders passed by different State Governments as also the Central Government with regard to the ceiling on the holdings, restrictions on movement of the stocks from one State to another, small scale industry reservations, mandatory use of Mandis etc., also constrain their use.

Though the provisions as contained in the respective State Warehouses Acts can act as a facilitator so far as legal enforceability is concerned, yet the Warehouse Receipt has not gained its acceptability over the years for there being no very strict quality certification parameters for the quality and quantity as contained in the Warehouse Receipt, being in place so far.

The other main reason for the Warehouse Receipts not gaining the acceptability is the lack of fiduciary trust on the part of banks and traders and this greatly restricted the number of companies which could act as warehouseman.

SUGGESTIONS AND RECOMMENDATIONS

With the accelerating process of globalization and liberalization, there have been major changes in the economic policies of the country in the recent past. These have resulted in removal of various restrictions as also removal of various storage control orders besides the mandatory use of Mandis etc. Further India is now a signatory to the WTO arrangements and GATT agreement. This will gradually push the country to more liberalized era. The public interventions in the matter of food grains trade are likely to go down immensely and the country would gradually witness the regime of reduced subsidies and handling of the food grains trade through the private channels with much ease and flexibility. This would significantly increase the demand for a fully negotiable Warehouse Receipt so as to allow free flow of goods trade without the physical movement and delivery of the stocks except by the end users. The Government of India having seized of the issue, has recently brought out a Central Legislation for making the Warehouse Receipt a fully negotiable instrument.

Various problems encountering the Warehouse Receipt System can be addressed by enhancing the status of Warehouse Receipts in law by creating a really effective system of regulatory oversight and by instituting a secured central electronic registry allowing for the tracking of all changes in ownership and liens. New legislation for making the Warehouse Receipt fully negotiable may provide for a necessary legal framework and legal force in order to facilitate better credit delivery, easy tradability and better credit flows which will ultimately help to boost the agricultural produce sector, but at the same time it is strongly felt that it would be absolutely necessary to provide for very strict quality certification parameters both for quality and quantity and a clear cut enunciated responsibility on the warehouse owner who should be required to display the creditworthiness and the trust of the highest order. More rigorous quality standards in comparison to those presently available are required to be put in place in order to ensure the quality maintenance over a sufficiently longer period of time. To enforce strictest quality standards both for quality and quantity at the warehouses, the required infrastructure as to the measurement of grades and standards need to be put in place, so as to reduce the chances of disputes on account of quality and quantity standards as also to improve the credibility of the Warehouse Receipt, thereby improving the fiduciary trust.

It should be essential for the warehouse owners to gear up appropriate market intelligence on the prices of various commodities linked with the grades/standards.

In view of the tremendously large number of commodities and within the commodities, large number of varieties, it may not be feasible to prepare for the specifications adequately for being able to conform to the quality standards in respect of all such commodities, grades and varieties. It would, therefore, be appropriate that to begin with, only few selected commodities and the selected varieties should be taken into the net of such rigorous quality standards for issue of Warehouse Receipts which could be easily traded with. As more and more infrastructure is added in order to ensure foolproof assessment of such standards, the additional commodities as also additional varieties, should gradually be added to this net.

Adequate publicity measures should be adopted so as to popularize and educate the trade and others to facilitate the general acceptability and easy transferability of the Warehouse Receipts.

Various barriers particularly the high level of public interventions in the market of food grains and sugar, tariffs on imports, storage control orders, mandatory use of Mandis, etc. need to be completely lifted or gradually liberalized in order to allow free flow of trade all over the country. The incidence of sales taxes or value added taxes or other levies should be attracted only once at the time of physical delivery for end consumption.

To generate a feeling of trust and confidence, there is a need for accreditation agencies which are capable of accrediting and certifying the warehouses in such a way that the warehouse structure and various operations in such warehouses meet the certain specified parameters.

To ward off the fluctuations in the prices in the market varying from place to place and from time to time, necessary safeguards need to be provided to prevent political interventions and that the markets play a role which is totally transparent where the prices are determined purely by economic factors.

REFERENCES

1. O.N.Chhibber "Warehousing Corporations in India".
2. Report of All India Rural Credit Survey Committee.
3. Negotiable Instruments Act, 1881.
4. Report of Inter-Ministerial Task Force on "Agricultural Marketing Reforms"
5. Manual on Systems, Procedures and Practices of Scientific Warehousing by the Central warehousing Corporation.