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October 4, 2001

Mr. Roger Hinkle  
Chief, Licensing Authority Branch, Warehouse and Inventory Division  
Farm Service Agency  
United States department of Agriculture  
STOP 0553  
1400 Independence Avenue, SW  
Washington, DC 20250-0553

*Re: Proposed Rule: "Implementation of the United States Warehouse Act," 66 F.R.  
46310 (September 4, 2001)*

Dear Mr. Hinkle:

The National Cotton Council of America (NCC) hereby submits comments on the proposed rule designed to implement title II of the Grain Standards and Warehouse Improvement Act of 2000 which amended the United States Warehouse Act (the "USWA"). The proposal would establish the rules governing the licensing of agricultural commodity warehouses under the U.S. Warehouse Act as well as rules governing the use of electronic warehouse receipts and other electronic documents related to sales and transfers of agricultural commodities. NCC generally supports the proposed rule, including its revisions to regulations governing federally licensed warehouses and its incorporation of rules for electronic warehouse receipts and other electronic documents.

The National Cotton Council is the central organization of the United States cotton industry. Its members include producers, ginner, cottonseed crushers, merchants, cooperatives, warehousemen, and textile manufacturers. While a majority of the industry is concentrated in 17 cotton producing states, stretching from the Carolinas to California, the downstream manufacturers of cotton apparel and homefurnishings are located in virtually every state.

The NCC offers the following specific comments with respect to the proposed rule and the sample agreements accompanying the publication.

#### **1. Structure**

In general, the NCC supports the overall structure of the proposed rule and its accompanying agreements. The NCC is concerned, however, that some important provisions governing licensed warehouses or the use of electronic receipts or documents that should be given universal application in the regulations have, instead, been shifted to

individual agreements. In addition, in at least one instance, the accompanying agreement contains a mandatory requirement that appeared to be discretionary in the regulation.<sup>1</sup>

It is arguable that some provisions that were placed in the accompanying agreements should be in the regulation. For example, with respect to the information required to be included on a warehouse receipt, the underlying statute states: “Each receipt issued for an agricultural product stored or handled in a warehouse licensed under this Act shall contain such information, for each agricultural product covered by the receipt, as the Secretary may require by regulation.”<sup>2</sup> However, the regulation does not spell out this requirement.

To the extent that the Department determines to finalize the regulation with the same fundamental structure as the proposed rule, the NCC recommends that a procedure for amending the accompanying agreement be developed and included in the regulations. Such a procedure should provide for an opportunity for notice and comment by persons likely to be affected by any such amendment.

## **2. Levying of fees**

Section 735.4 of the regulation sets out general authority for the charging of fees by USDA. However, neither here, nor in other provisions concerning fees contained in the proposed rule or in the accompanying agreements, does the authority reference the statutory directive that the fees be designed to “cover the costs of administering this Act.”<sup>3</sup> We recommend that section 735.4 be amended to include this statutory limitation on fees.

## **3. Arbitration**

Section 735.9 states that disputes under the Act “may be resolved by the parties involved through mutually agreed upon arbitration procedures.” This provision is consistent with section 16 of the USWA. However, section 735.9 goes further and provides authority to proscribe different rules concerning arbitration in the applicable licensing agreement. The included cotton storage licensing agreement contains an arbitration provision that is mandatory with respect to disputes concerning delivery of cotton from a warehouse. This example highlights the NCC’s concern over the structure of the regulation and agreements. Section 735.9 implies that arbitration is discretionary, yet the accompanying agreement makes it mandatory in certain instances. The NCC recommends that the position of the regulation on arbitration be clarified and that care be taken to ensure that provisions in the accompanying agreements do not run counter to the general rule as expressed in the final regulation.

## **4. Warehouse receipt requirements**

Section 735.300 sets out certain requirements for warehouse receipts. Section 735.300(a) omits any direct reference to information required to be contained on a receipt.<sup>4</sup> The structure of subsection (a) also makes the mandatory and discretionary parts of that subsection somewhat unclear as to their scope.

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<sup>1</sup> See item 3 below.

<sup>2</sup> Section 11(c) of the United States Warehouse Act (7 U.S.C. 250(c)),

<sup>3</sup> Section 4(a) of the USWA (7 U.S.C. 243(a)).

<sup>4</sup> See section 11(c) of the USWA and discussion above at item #1.

The NCC recommends that subsection (a) be revised to clarify its scope and intent and suggests the following revision:

*(a) Warehouse receipts:*

*(1) must comply with the requirements of the Act and be in a format approved by DACO;*

*(2) may be negotiable or non-negotiable; and*

*(3) may be in a paper or electronic format.*

Even with this change, this subsection does not make a direct reference to “information” that is to be on the receipt. The NCC encourages USDA to make a more direct reference to “information” on the receipt at this place in the regulations. The NCC also encourages the agency to consider whether a more detailed statement of warehouse receipt information in the regulation is required by section 11 of the USWA.

### **5. Section 735.302 Electronic warehouse receipts (EWRs)**

The NCC has several concerns about section 735.302 and its relationship to section 735.300(a) and to certain sections of the accompanying agreements.

In general, the proposal does not appear to fully incorporate an important premise of the revised USWA – that warehouse receipts may now be issued in paper or electronic format. While section 735.300 clearly states as much, section 735.302 describes electronic receipts as an “option” and names them EWRs. The first sentence of section 735.302 seems to be a redundancy.

The accompanying agreements seem to further undermine the effort to fully incorporate electronic receipts into the warehouse system. In the licensing agreement for cotton, for example, Section IV.N. is entitled “Warehouse Receipts,” and yet the entire section deals with a warehouse operator’s responsibilities concerning EWRs.<sup>5</sup> The next section is headed “V. Paper Warehouse Receipts,” and yet seems to deal with both electronic and paper receipts in some parts and only paper receipts in other parts. Further, it is only in section V.B. of the licensing agreement for cotton that information required to be on the receipt is spelled out. It is not clear in context, however, whether this requirement applies to paper receipts, electronic receipts or both. There are numerous references throughout section V. to “written or printed terms” or “printed or stamped.”

The NCC encourages the agency to review its structural approach to incorporating electronic formats into the normal warehouse receipt system. It would seem more appropriate for the regulation and the accompanying agreement to describe common requirements for receipts in general, and then specifically break out requirements only applicable to electronic receipts and those only applicable to paper receipts.

The NCC also recommends that the statement of nondiscrimination of EWRs and the treatment of a holder of an EWR be more directly stated in the regulation. It is unclear to

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<sup>5</sup> Note also that section V.N.1. applies when the warehouse operator is “choosing the option to issue Electronic Warehouse Receipts (EWRs) instead of paper warehouse receipts.” There appears to be no reference to such an “option” in the agreement. The “option” reference, therefore, must refer back to the regulation – but this is unclear.

the NCC whether the statement that an EWR “possesses the following attributes” is an appropriate way to convey the legal standing of EWRs issued in accordance with the Act.

The NCC recommends that section 735.302 be amended as indicated below:

*(a) Warehouse receipts issued in electronic format are referred to as Electronic Warehouse Receipts (EWRs).*

*(b) Warehouse operators licensed under the Act and warehouse operators not licensed under the Act may issue EWRs for the agricultural product stored in the warehouse.*

*(c) Any warehouse operator choosing to issue EWRs must:*

*(1) Only issue...*

*(2) Inform DACO ...*

*(3) Before issuing ...*

*(4) When using ...*

*(5) Cancel an EWR ...*

*(6) Correct information ...*

*(7) Receive written approval ...*

*(8) Notify all holders ...*

*(d) An EWR establishes certain rights and obligations with respect to an agricultural product stored in the warehouse that issued the EWR.*

*(e) The person identified as the ‘holder’ of an EWR will be considered to be in possession of the EWR.*

*(f) Only the current holder of the EWR may transfer the EWR to a new holder.*

*(g) The identity of the holder must be included as additional information for every EWR.*

*(h) Only one person may be designated as the holder of an EWR at any one time.*

*(i) An EWR may not be issued for a specific identity-preserved or commingled agricultural product lot if another warehouse receipt representing the same specific identity-preserved or commingled lot of the agricultural product is outstanding. No two warehouse receipts issued by a warehouse operator may have the same warehouse receipt number or represent the same agricultural product lot.*

*(j) An EWR may only be issued to replace a paper warehouse receipt if requested by the current holder of the paper warehouse receipt.*

*(k) Holders and warehouse operators may authorize any other user of their provider to act on their behalf with respect to their activities with this provider. This authorization must be in writing, and acknowledged and retained by the provider.*

*(l) A depositor or current EWR holder may request a paper warehouse receipt in lieu of an EWR.*

*(m) A warehouse operator that is licensed under State law to store agricultural products in a warehouse and who elects to issue an electronic warehouse receipt under State law does not issue such receipts in accordance with this subpart.*

Section 735.302(b)(7) provides a very broad authority to authorize others to act on the behalf of a holder of an EWR. That paragraph also appears to enable warehouse operators to authorize others to act on their behalf. The NCC is somewhat concerned about the breadth of this paragraph and the possibility that may enable a warehouse operator to authorize someone else to issue EWRs with respect to cotton stored in its warehouse. It is unclear whether the paragraph would prohibit a warehouse operator or a holder to authorize the system provider to take certain action on their behalf as the power to authorize another appears to be limited to “user(s)” of the provider.

## **6. Electronic providers and electronic documents**

It is unclear what the regulation establishes with respect to electronic documents other than electronic warehouse receipts. We were unable to find any reference in the regulation to section 11(e)(4) of the USWA as it applies to electronic documents.

Although the regulation purports to establish oversight of systems in which electronic documents will be transferred, it does not indicate the legal status of any such electronic document – with the exception of electronic warehouse receipts.

The requirement of a \$10 million net worth applicable for a provider agreement to establish a system to issue and transfer other electronic documents should be carefully examined. It is not clear what risks this net worth requirement is designed to help offset. The NCC recommends that the agency review this net worth requirement and tie it more closely to the type of electronic document, and corresponding risks, that are to be undertaken by the system provider.

## **7. Cotton warehouse licensing agreement.**

Under section II.B.1. of the cotton warehouse licensing agreement, all warehouse operators must submit financial statements within 90 days of the close of the fiscal year. The NCC suggests that this deadline be increased to 120 days.

The NCC does not understand the meaning of the reference to “non-licensed cotton” and “licensed cotton” in section IV.A.3. of the cotton warehouse licensing agreement.

The NCC recommends that the agency review the structure of section IV.N. and V. as discussed previously. Further, the NCC notes, for example, that section IV.N.2. states that the warehouse operator “will ensure that an issued EWR establishes the same rights and obligations with respect to an agricultural product as a paper warehouse receipt....” Can the warehouse operator make such assurance? Whether the EWR establishes the same rights and obligations would seem to be a matter for the applicable State or Federal law. The concept that the EWR shall have the same legal status as a paper receipts would seem to be a provision more appropriately relegated to the published regulation.

The previous recommendations concerning section 735.302(b) of the regulation are also applicable to this portion of the cotton warehouse licensing agreement. The NCC

recommends that the structure of section V. Paper Warehouse Receipts be reconsidered to better incorporate electronic and paper requirements.

#### **8. Information on EWRs**

The NCC notes that in the Addendum to the Provider Agreement to Electronically File and Maintain Cotton Warehouse Receipts, it is stated that “It is each individual warehouse operator’s responsibility to supply the necessary data to complete each element.” While the NCC agrees with this statement, we are unsure to what extent such a statement in the agreement with the system provider can bind warehouse operators. We encourage the agency to review both the regulation and all accompanying agreements to ensure that warehouse operators licensed under the Act and those not licensed under the Act that wish to issue EWRs are required to supply the data necessary to issue an EWR.

#### **9. Use of New York law**

The NCC is unsure why the proposed rule seeks to establish New York law as the applicable legal precedent under the regulation. This choice of a jurisdiction may be confusing to companies throughout the United States that are familiar with their own commercial laws. The cotton electronic warehouse receipt system has operated for several years without a specific jurisdiction’s laws being imposed on that system.

We appreciate the opportunity to submit these comments.

Sincerely,

William A. Gillon  
General Counsel and Director of Trade Policy