

Thank you, Bian, it is indeed a pleasure and an honor to be with all of you as we examine many aspects of Soybean Trade and Risk Management. The opportunity to work the China Chamber of Commerce for the Import and Export of Foodstuff, Native Produce and Animal By-products (CFNA), The United Soybean Board (USB) and the American Soybean Association (ASA) in this conference is as important as any event I will attend this year. Thank you for hosting the conference and for our continued work together.

In my role with the North American Export Grain Association, my primary responsibility is to achieve a mission that seeks to promote and sustain the export of grain and oilseeds from the United States. In doing so I am guided by our objective of working jointly to foster a grain and oilseed export industry that provides the best environment for all stakeholders – from producer to consumer. Importantly our mission and this objective are founded in NAEGA Membership's commitment:

“to integrity in a commercial environment supported by free trade and competition in commerce involving grain and other agricultural products; to eliminate abuses relative thereto; to eliminate or secure freedom from unjust, unlawful and oppressive exactions in commerce; to promote certainty in the customs and usages of trade and commerce; to promote a more enlarged and friendly exchange among persons engaged in business; and to cooperate to the fullest extent practicable with all governments, governmental departments, governmental and private corporations, partnerships, associations and groups with an interest in providing for global food security and efficient international commerce.” (NAEGA By-Laws)

While my primary purpose in being here is to review the critical importance of contract sanctity with a system of commercial arbitration as the primary source of dispute resolution, I want to first take a moment to congratulate those of you involved in the provision of food here in China. The importance of your work really cannot be overstated. The success of your businesses is critical to China's continued economic progress and food security.

In its 1997 report: “**China 2020 Food Security Options, AT CHINA'S TABLE**”, the World Bank included among key required initiatives for China to “Reduce government intervention in the cereal and fertilizer sectors, encourage market-determined prices, and open marketing and trade competition.”

In many ways the conference should be celebration in China's success in these initiatives. Success in meeting its food security needs. And success, with the assistance of commitments under the World Trade Organization accession agreement, in opening its food and fiber markets to important global trade opportunities. Certainly the Chinese Soybean Crushing industry has played a major role in this success.

Our meeting is also an opportunity to acknowledge China's role in the global economy and society and the progress in Sino US relations. In what was likely one of his last public interviews, Deputy Secretary Richard L. Armitage, US Deputy Secretary of State said "..... we should welcome a larger role (for China in the World's community). Where we are right now ..... is where Chinese leaders and U.S. leaders say, (is) the best relationship we've ever had with China. And the peaceful rising of China .... Will be the most momentous in the first half of this century. (China) is so big. And not just in terms of land size or population, but they're so big in terms of the energy they require, the raw materials they require, their reach, what they'll do as they take a correct place on the world stage that I think it will be momentous." (As aired on PBS in an interview with the Charlie Rose, Washington, DC. December 10, 2004).

As a former staff member of Ambassador Armitage, I have often admired his straightforward diplomacy. His statement, I believe, provides important background for the conference and my discussion regarding Contract sanctity in international agricultural product trade.

Today, I hope to reinforce the commitment of all buyers and seller of soybeans to sound commercial practice starting with sanctity of contracts as a fundamental concept that makes international trade possible. I think the logic is simple and that we should acknowledge the fact that if trade operating in a given market, under a set of common laws and enforcement has the reputation of regularly defaulting on contracts, then the cost of those contracts will rise in relation to current market prices. Ultimately the increased cost of doing business in that market, will negatively impact on investment, the economy and food security in that market. If a market is burdened by a reputation of non-performance against contracts, not only will the costs of imports increase but the political reaction to these conditions will result in increases on trade barriers for exports. Any discussion of risk management in international markets should emphasize sound commercial practice and contract sanctity as the priority.

My entire professional career has involved the trade of grain and oilseeds. It is clear to me that international grain and oilseed trade functions best as an open network, ubiquitous with accurate price data and other vital market information. Participants in the trade, utilizing transparent market information, serve one-another by producing a commodity, adding value to it, offsetting price risks, protecting the commodity's value, shipping commodity for further processing, food and animal feed. This system is further best supported by a cost effective, and enforceable system of commercial arbitration to provide for dispute resolution. Ultimately our products and trade provide for a significant and indispensable contribution to national and global food security.

Participants in the international trade which moves grain and oilseed from the production field, through a series of transportation, quality maintenance and official requirements to commodity end users around the world, must share the norms or values of fairness, truth, and reciprocity beyond those customary to many market transactions. International trade in perishable agricultural products that are the subject to strongest of political influences, the provision of man's basic need for food, demand the highest level of trade sophistication. That is why our business is conducted on a different basis from other industries. In such a system it is essential that rules be complied with, that trades be fair, and that disputes be resolved through impartial arbitration that is affordable to the participants.

While there are several models of contracts and forms dispute resolution in global grain and oilseed trade, our industry carries with it the obligation to adhere to a set of well-established principles grounded on the assumption that the corresponding party will honor his contract, resolve disputes through amicable negotiations, or submit the dispute to a recognized and impartial industry arbitration fora. When patterns of trade change as the always have in international trade of grain and oilseeds, there is a need to review and re-emphasize this obligation.

I have observed two conundrums that often exist within new participants to the trade:

1. If a high level of sound commercial practice and contract sanctity is the best for all participants in the trade then why do we experience serious, large scale and costly failures to preserve contract sanctity? And
2. If commercial arbitration is the most efficient, expedient, fair, and least expensive manner to resolve a dispute then why do we find many participants in the world's emerging markets are reluctant to make use of this relatively simple and informal process designed by participants in the industry to quickly resolve differences without resort to the expensive and protracted process of litigation? And why do we often have difficulty from the failure of new market participants to honor contractually agreed upon arbitration awards?

These issues must be resolved to assure that the principal participants in the market - the producers, merchants, and end users can survive and compete. A resolve to observe and maintain contract sanctity and an effective arbitration system is imperative not only to the performance of the market but also to assure that non-contract performing participants in the market do not receive a competitive edge over their colleagues who honor their contractual obligations.

It is essential that all market participants embrace a proven dispute resolution system. Qualified members of the industry who have no commercial interest or connection with either of the disputing parties conduct the industry arbitrations. The arbitrators are fully familiar with the rules, customs and practices of the trade and they strive to ensure that the dispute between the parties is resolved fairly so that the trading system can continue to function with the necessary high level of integrity. Simply put, there is no better way to remedy a misunderstanding or to right a wrong in a business transaction.

Though the obvious benefits of arbitration are long recognized throughout the world, there are those still to be convinced within the trading system, particularly some in the emerging markets. It is imperative that those who question a trading system, and its established rules, based on centuries of successful fair trade, are convinced that such a system serves the best interest of all. It enables us to sell and purchase grain and oilseeds from international markets at competitive prices by locking in such prices well in advance of delivery with the guarantee of payment and/or delivery.

I think it important to examine the overwhelming acceptance and use of arbitration throughout

the world.

### **The United Nations New York Convention – International Acceptance of Arbitration**

On June 10, 1958 the delegates to the United Nations ratified the provisions of the Convention on the Recognition and Enforcement of Foreign Arbitral Awards (New York Convention). The signatories ratifying this treaty and the countries adopting its provisions agreed to recognize and enforce “arbitral awards made in the territory of a State other than the State where the recognition and enforcement are sought, and arising out of differences between persons.” “The term ‘arbitral awards’ shall include not only awards made by arbitrators appointed for each case but also those made by permanent arbitral bodies to which the parties have submitted.”

The essential provision of the Convention requires that:

“each Contracting State [nation] shall recognize an agreement in writing under which the parties undertake to submit to arbitration all or any differences which have arisen or which may arise between them in respect of a defined legal relationship, whether contractual or not, concerning a subject matter capable of settlement by arbitration.”

Further, “the term ‘agreement in writing’ shall include an arbitral clause in a contract or an arbitration agreement, signed by the parties or contained in an exchange of letters or telegrams [telexes, facsimiles or e-mail].

The UNCITRAL Model Law on International Commercial Arbitration (Model Law) defines an arbitration agreement as follows:

“Arbitration agreement” is an agreement by the parties to submit to arbitration all or certain disputes which have arisen or which may arise between them in respect of a defined legal relationship, whether contractual or not. An arbitration agreement may be in the form of an arbitration clause or in the form of a separate agreement.

The arbitration agreement shall be in writing. An agreement is in writing if it is contained in a document signed by the parties or in an exchange of letters, telex, telegrams or other means of telecommunication which provide a record of the agreement, or in an exchange of statements of claim and defense in which the existence of an agreement is alleged by one party and not denied by another. The reference in a contract to a document containing an arbitration clause constitutes an arbitration agreement provided that the contract is in writing and the reference is such as to make that clause part of the contract.

The New York Convention and the Model Law provide a framework for the international trade in agricultural products to resolve disputes through arbitration and to have the awards, rendered by the arbitral body, enforced in the domiciliary country of the losing party.

Currently, 134 countries have agreed to participate in the New York Convention and have ratified the treaty. China is party to the Convention.

In the United States, Trade Rules, Model Contracts and arbitration systems for grain and oilseed trade are maintained through grain and oilseed trade associations. Our National Grain and Feed Association system applies to domestic trade (beginning with first purchases from producers) and rail freight. NAEGA has a model contract and arbitration that applies to F.O.B contracting

for vessels shipments only.

I am sure you are aware of the GAFTA and FOSFA systems that apply in international trade. I believe they will be discussed by others at this conference.

If you would like to further examine the very successful US system, please contact me or visit the NGFA website: [www.ngfa.org](http://www.ngfa.org) and the NAEGA website: [www.naega.org](http://www.naega.org)

### **Factors Contributing to Defaults – An opportunity to address problems**

It is obvious that a number of factors influence defaults, including business practices or customs regarding contractual obligations. Other problems include restrictive currency regulations that inhibit hedging and in some cases outright prohibitions against hedging, and lack of familiarity with international trading rules and arbitration procedures along with the consequences of failing to comply with these universally acceptable precepts. Most importantly all trade participants must be adequately financed to insure contract integrity can be maintained.

Government Actions: I would like to take a few moments to reflect on problems caused by inappropriate governmental actions. As I hope you are aware, NAEGA, the National Oilseeds Processors Association and Trade Associations representing the trade from Brazil and Argentina are very concerned about the regulatory and enforcement actions of the Chinese authorities. We are ultimately concerned that the uncertainty that results from enforcement of official requirements that, contrary to WTO obligations; do not recognize the need to facilitate trade; are not based on sound science; and lack necessary transparency and advance notice, encourage a lack of contract sanctity.

As an example, I would like to point out concerns with AQSIQ DECREE 73:

On June 16, 2004, China's quarantine and inspection agency, the General Administration of Quality Supervision, Inspection, and Quarantine (AQSIQ), issued revised regulations for importation of soybeans and other products subject to the quarantine process, which became effective on July 1, 2004. The new regulations, known as Decree 73 (Items on Handling the Review and Approval for Animal and Plant Entry Quarantine), were not properly notified to the World Trade Organization (WTO). To date, China has yet to properly identify, as well as support scientifically, the phytosanitary risks that require implementation of such regulations. In our estimation, Decree 73 places exporters in an unfavorable commercial position relative to domestic producers in China.

While Decree 73 extended the validity of quarantine import permits (QIP) from 3 months to six months in accordance with an agreement reached during the April 2004 meetings of the U.S.-China Joint Commission on Commerce and Trade (JCCT), Decree 73 included additional burdensome requirements that constrain U.S. exporters' ability to export grain and oilseeds to China, and that create uncertainty for U.S. producers.

Following are NAEGA's major concerns with Decree 73:

Requires exporters to assume the risk of non-compliance with Chinese laws. Decree 73 requires all contracts for importation of soybeans and other products to include Chinese inspection and quarantine requirements as a contract term. Further, the contract must stipulate that entry of goods is dependent on whether the goods comply with relevant Chinese laws and food safety regulations. Such requirements are inconsistent with standard international trading practices in that exporters of agricultural products are forced to assume the risk of non-compliance with foreign standards. Even Chinese exporters do not face those requirements in export markets. Under an international commercial sale, the quality, condition, and specification of the goods are determined when the goods are shipped, and therefore, the risk is transferred from the exporter to the importer upon shipment of the product, not upon discharge in the foreign port. Under these requirements, the importer can reject shipments if the Chinese authorities determine the product does not comply with Chinese laws, creating a great deal of uncertainty for U.S. suppliers.

Creates zero tolerance level for GMO presence. Decree 73 requires that a safety certificate issued by the Ministry of Agriculture in China accompany all products of Genetically Modified Organisms. The Ministry only makes certificates available for GMO products that are approved by the Chinese government. The requirement in essence creates a zero-tolerance requirement for any shipments that contain trace elements of non-approved GMO products. Zero-Tolerance standards that apply to many commercially produced agricultural commodities are impossible to meet. The failure to provide for the adventitious presence of GMO events in any shipment results in the strong possibility that trade will be prohibited.

QIP applications require identification of supplier. It is not practical to require the importer to list the supplier at the time of application because often the supplier is often changed after the QIP is issued. The exporter is the contracting party with the Chinese importer, not the supplier.

Allows for arbitrary revocation of QIPs. Chinese authorities can, at any time, invalidate an import permit in the event of any announcement by the government that forbids entry of the product. Basically, this regulation provides Chinese authorities the license to issue scientifically unfounded bans on U.S. exports of agricultural products, which runs counter to China's obligations under the WTO SPS Agreement and the GATT 1994.

While it is difficult to estimate the costs and implications of these sort of official actions it should be made clear that while trade and investment is occurring under more uncertain conditions, it is occurring with higher risk premiums built into the existing contracts. I think most of us are aware of one of the most obvious costs when regulations prevent vessel discharge. The potential holdup costs from such circumstances would be astronomical. Depending on the size of cargo and port of import, demurrage charges from re-directing a vessel to an alternative destination, quality deterioration and other costs could add up to millions of dollars per held-up vessel.

It is also important to recognize the impact that increases in market volatility that result for even short term disruption of trade that results from inappropriate official enforcement actions. In the US we certainly appreciate the assurances that Chinese officials have provided to our senior U.S.

trade officials that Decree 73 will not disrupt U.S. soybean exports to China. However assurances do not remove the risk created by the existence of regulations like Notice 73. For example, the recent problems with shipments of soybeans from South America have had secondary effects on our marketing. Rejection of products from Brazil and Argentina send the U.S. market into a tailspin in terms of price declines created by an unsuspected glut of additional product in the world market. Our consistent experience is that, contrary to such assurances, the short term disruption of trade that results from the combination of an interest in managing trade and the authority described in Decree 73 is not only expensive but can result in the reputation that a market is unreliable. As I discussed earlier, the avoidance of this reputation is important to all market participants.

### **Working Together to Improve Trade**

Market participants must acknowledge and address each of these factors. Further, the individual merchants or their trade organizations should consider undertaking a comprehensive and large scale educational effort to familiarize the market participants and government officials with the prevailing trade rules, the protections and expectations of those rules. Governments in particular must be educated to understand the impact of regulation on trade.

Membership in the World Trade Organization (WTO) brings with it the reciprocal responsibility of adhering to its contractual responsibilities given the extraordinary market privileges inherent in WTO membership. China's entry into the WTO provided it with new trading opportunities that resulted in immediate and significant market growth in much of the developed world's consuming markets. Further, when governments determine the credit policy any denial of credit to a private sector has a direct impact on the efforts to perpetuate sound commercial practice and contract sanctity.

In closing I want to urge our joint actions to work to expand our common understanding and improve conditions of trade. In the event of disputes, we should all work to ensure arbitration awards are honored. Here in China, as in the rest of the world, regulatory measures must meet WTO standards, necessary financial controls must exist and financing must be provided to allow industry to perform on contracts.

Let us remember:

There are practical limitations to trade in bulk agricultural commodities.

Food Standards often cannot and should not be applied to commodities for feed or further processing.

Zero tolerance is not practical nor possible.

Risk does exist – this conference is to discuss risk management not the impossible of risk elimination.

Origin determination of quality and safety factors is superior tool to manage risk.

Thank You, I look forward to our ongoing discussion.

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For the Sino US Trade and Risk Management Conference, January 13- 14 2005, Beijing, China