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**Paving the Way Forward for Rural Finance  
An International Conference on Best Practices**

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**Discussant Reaction Paper**

**Commentary and Reaction to Theme Paper**

**Legal and Regulatory Requirements for Effective  
Rural Financial Markets**

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These comments reflect the views of Jolyne Sanjak and not necessarily those of USAID.

The authors have put forward a very useful, comprehensive diagnostic of the legal and regulatory issues that need to frame efforts to evolve rural financial markets, and in fact, financial markets in general. The authors should be congratulated on an excellent paper. Herein, I make some critical observations regarding their perspectives on “land titling” and related legal and institutional considerations (note, I am choosing not to comment much on the content of the paper much beyond the legal and regulatory issues raised relating to this sub-theme). Clarification of the issues is important especially because the paper clearly reinforces my view that there is a fertile ground for working at the nexus of our respective interest areas – rural finance and good governance of property rights.

### **Some Overarching Considerations**

On p. 24 you state: “Land-use rights are necessary but not sufficient conditions for access to credit based on land use rights. Land titling and cadastres are neither necessary nor sufficient conditions for using land-use rights as collateral.” This statement is problematic although not entirely incorrect. Drawing on the many points in the paper with which I agree and as a preview to my perspectives, I propose the following alternative view: *Effective property rights systems – comprising laws, institutions, and information systems harmonized with local practice and custom – are necessary but not sufficient conditions for improving access to credit. Cadastres are not needed for secured lending, however, parcel based GIS that includes physical and legal attributes of property have multiple other uses and should mean lower transactions cost in collateral-based lending. These systems have the potential to make information more reliable and easier to obtain, thus, making it easier to understand and price risk. This is especially important where court systems are neither efficient nor equitable and where access to and quality of information on real property has been problematic (with fraud and corruption being all too frequent). Regularization of legal records is necessary – formal recognition and recording of informal/extra-legal property rights (including rights of ownership, use and transfer), resolution of competing claims and other irregularities and issuance of first title or adjudication of rights are among the actions that will create a reliable information systems. And, regularization, recordation and use in transactions must be grounded in an appropriate legal and regulatory framework. Still, this ‘infrastructure’ is not sufficient to expand rural credit. There are legal and regulatory issues to address to enable the use of property as collateral.*

Throughout the paper, and especially in the executive summary, the manner in which the authors portray ‘land titling’ efforts reflects some misconceptions. The view of donor supported interventions is too homogenous with some stereotyping from now out-dated approaches. Greater understanding of work on land administration and title regularization (new terminology in which land titling is an element) would benefit the authors work. The current portrayal is similar in generalization to the way the some folks would say the microfinance programs are just non-sustainably supporting NGOs that are giving bits of cash to very poor people and their microenterprises – not realizing that such programs *are* broader and *have* evolved toward sustainable contributions to development of broadly accessible, innovative financial products and to an improved regulatory environment. ‘Land titling’ programs have also evolved! In fact, the alternative view above, reflects an emerging consensus among the ‘community of practice’ that is working to achieve reforms in the area of ‘land titling’ and has already begun to influence

improved project design (and, in fact, derives from ‘best-practices’ review of projects already underway). Moreover, the authors do not seem cognizant that much of the specific concerns about the legal framework governing ownership and use of real property has been and is being said also under the rubric of land policy and land administration. For example, the discussion on page 9 on conflicts among laws, fragmentation across them and gaps in coverage of transactions both in regulation and in formal information has been in the cache of key points used by myself and several of my peers for a while. Achieving reform is a process with a number of constraints – lack of awareness by senior policy makers, constraints on including reform of law in they type of loans used by MDBs, and vested interests that like things the way they are.

### **Counterpoints, Clarifications, and Additional Points<sup>1</sup>**

***‘Land Titling’ Programs Have Evolved to be More Holistic:*** Prior to mid-1990s, stand alone agrarian land titling programs as well as redistributive land reforms were implemented. Often these involved the creation of cadastral maps but rarely involved the property registry. Justifications included social and economic impact of improved tenure security and privatization of public property. These programs did not address issues in the enabling environment that connects title to market (e.g., for credit access) and often did not consider the capacity and accessibility of the property registry and cadastre. This lack of foresight limited the impact and sustainability of these efforts. Today, these problems are increasingly being addressed through a more comprehensive framework for project design – Land Administration. Registry and Cadastre modernization, title regularization, conflict resolution and appropriate legal and regulatory frameworks are all relevant under this broader rubric. Still, there *are* more narrow – spatially and in scope -- land titling projects that focus on specific contexts with immediate needs. For example, USAID has funded land titling of housing constructed with its funds during the recent earthquake reconstruction in El Salvador. USAID funds land titling and conflict resolution in the context of several environmental conservation projects in hopes of creating better incentives for good stewardship. In Moldova, USAID funded a relatively simple and low-cost title and registration effort with the purpose of facilitating financial transactions after farm privatization that included legal aid and work on the legal framework for mortgage lending to allow more immediate results. These are not incompatible with more holistic approaches. Increasing donor coordination means better synchronized projects which feed into and build from one another.

While Hernando de Soto has criticized ‘land titling’ projects, his work does not imply that ‘land title’ is not a useful tool or that title, in and of itself “does violence to traditional and transitional economies.” Through his diagnostics, writing, and approach to reform – “property formalization,” de Soto stresses the need for understanding of the informal rules of the game for allocation of rights through ‘bottoms-up’ participatory approaches and of the importance of comprehensive legal, institutional and informational reforms to connect the poor and informal

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<sup>1</sup> *These are not given in any particular order and for the sake of brevity are not complete in coverage or in articulation in this draft. These points are made in the hope of beginning to engage in a more constructive conversation and creating a space for synergies.*

economic actors to the process of economic development. De Soto has transformed the optic through which newer projects are being designed from agrarian reform to an asset lens.

There is now broad recognition of the need to start from reality – ‘the broad spectrum of rights actually in use’ and there are some very good examples in practice in LAC (and, I am sure, elsewhere): Peru’s success built from Hernando de Soto’s work, the titling of the Izoceno indigenous territory in Bolivia, El Salvador’s post-war resettlement process and recent decision to register rental contracts, etc.<sup>2</sup>

**‘Titling’ is Not Synonymous with Fee Simple Individual Ownership:** Titling is a tool to formally record rights adjudicated, assigned or acquired. These can be individual or group rights and can have restrictions on use. Historically, there has been a preference among policymakers for the fee simple, individual title modality. Today there is a much better appreciation of the many types of effective property rights. There are ample examples in which titles have been issued to other than fee simple ownership forms — title to agrarian reform cooperatives in name of the cooperative as a legal person, with or without share stock certificates for individual members and with or without restrictions on transfer; titling the perimeter of an indigenous territory wherein individual rights are governed by custom and not formally recorded and where ownership is not alienable; family titles in which each member is formally and fully co-owner with the other (título proindiviso). Use rights obtained through various contracts are not subject to title but can be registered e.g., deeds recognizing rights to use municipal land (escritura de dominio util), rental contracts, etc.

Title in and of itself does not ‘do violence to traditions in transitional or traditional economies.’ This reputation results from *processes* that were top-down, that (benignly or out of malice) forced one type of title regardless of custom, tradition, etc. Examples include cases in African where fee-simple ownership titles were imposed over customary rights, cases in Latin America of agrarian reforms in which collective titles were imposed over individual informal/customary rights, situations where one group was awarded title as another was driven out, etc. Today, that genre of projects or approaches are quickly losing ground if they haven’t already been replaced by more flexible and participatory approaches.

**Regarding the Illustrations of Use Rights:** Important examples, e.g., Watergate, London, Hong Kong, of ‘successful’ use of land-use rights are given which offer lessons both on the financial services side and the land tenure side of this discussion, especially since there is a growing receptivity to giving more attention to rental and lease as options for the poor to access land for farming. However, not enough information is provided about key details of the context and of the mechanics in relation to secured lending to allow understanding of the lessons these examples might offer. Also, there might be some important limitations to the relevance of these examples.

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<sup>2</sup> The authors point to Bolivia to support many of their points and it does illustrate these points. However, in my view, Bolivia is not at all a representative example of the state of the art in land-title related interventions and can not be used to generalize.

An extraordinarily high value location might not be relevant to rural finance contexts we target. The kinds of cooperative arrangements and state leases differ from those typical in LDC rural areas (where production cooperatives have been common and condominium law is not so common). One wonders, also, do the tenants of religious organization land on Wall Street secure credit with the land or with the improvements they make on it? If the land-use rights in this instance serve as collateral, how does that work? Finally, we must note that the land in these examples has uncontested ownership and clearly defined rules for assignment of use rights backed by an effective judicial system. It would be useful and interesting to know the mechanics of these examples, including the case of Vanuatu, Papua New Guinea and Samoa.

***On Cadastre:** You state that “A cadaster system has a variety of useful purposes: zoning, tax collection, and land use planning. However, these potential useful features of a cadaster need to be balanced against their costs and the reality that most developing countries do not tax land.”*

The ***need [for benefits] to be balanced against their costs*** is an issue that is keenly on the agenda in discussions about best practices in land administration. Today, sustainability is a key consideration where it was not in the 1980s. There has been a worldwide debate on this theme over the last year and a half. This debate had not been well-informed by actual comparable data. An attempt to make available a more systematic framework for evaluating costs against benefits and to look across projects and countries was commissioned as part of a consultative project lead by the World Bank but with broad participation across donors.

Evaluation of cost/benefits is highly context specific and generalizations tend not to be valuable. What is included in coming up with costs estimates, units of measure, etc are not at all harmonized across examples. Contexts differ on a number of facets such as level of market integration, legal framework and institutional capacity, level of conflict and past corruption, quality of services, level of centralization, etc. Investments must be evaluated within a relevant time-frame (immediate needs and longer-term visions) and against multiple objectives (economic, environmental and social). Costs of technology, decentralization and a growing receptivity to outsourcing and using local talent all contribute to declining costs.

In the example given on Romania, you ask ‘Can countries afford property registration at this cost?’ Pro-rating based on initial project investments is not likely so useful. There are big front end investments in ‘infrastructure’ that later improve the cost and pace of title regularization. This implies that ultimately the per title registered cost would not be as high as the pro-rated calculation would suggest (IDB’s Peru rural land titling program is a good illustration in which the per unit cost are now under \$47 – including all the geospatial data investments.) There is early evidence that investments in land administration can be self-sustaining and even profitable if well designed. In El Salvador, the big loan from the World Bank is being paid back directly by the National Registry Center by the proceeds from more efficient services it provides (other examples can be found too -- Canada, Washington, D.C., ... )

Finally, with regard to the “... ***reality that most developing countries do not tax land.***”

This reality is changing as decentralization sets in and creates new demands and new space for more rational discussion of property taxation. (Ironically, the same logic applied to rural finance would mean, why bother having this event!)

***On systems that “penalize small rural land-use rights:”*** The high transactions costs (time and money costs) that affect disproportionately poor people and small farmers – and also put a damper on market transactions for all people --were/are largely due to centralization (location of institutions, requirement for signature by the country president or a cabinet member), very bureaucratic processes (e.g., 127 or more steps to title and even more to register in pre-reform Honduras), monopolistic set-ups, notarial requirements, clerical functions being handling by courts, and inefficient information (filed by person, non-automated, incomplete and without quality control). This is widely known, improvements have been made and progress continues to reduce such ‘penalties’ by administrative simplification, decentralization, etc. *within the title-registry-cadastral framework*. Additionally relevant but not so well acknowledged are the time and money costs associated with inefficient systems of issuing and accessing birth certificates and marriage certificates that the authors refer to in this paper and that encumber titling processes.

***Application of rules of priority:*** In this section, as throughout the paper, you make suggestions that are good but *dependent* on reliable and accessible information and enforceability of contracts. There should be mention of capacity of judicial system to enforce and more on the role of non-judicial dispute resolution. What issues that arise from inequitable access to the court system and reliability of the information contained in the registry system? Would such considerations give more value-added to modernizing information systems? Under any of the systems that you discuss, there will be implementation problems that emanate from poor governance of property rights. For example, while registry experts<sup>3</sup> stand by the principle of ‘first in registry, first in right,’ this principle can lead to conflict and confusion when applied to underdeveloped and poorly managed registries ( e.g., fraudulent registration superceding legitimate rights, abuses of adverse possession (titulo supletorio) or of family lands situations). Also, publicity works well when information is widely accessible but this should not be presumed. (Note: in LAC, property registries can be national, state, or local but access tends to be concentrated to national capitals and/or state capitals.)

Technical excellence in registry can not compensate for inadequate legal and regulatory framework, agreed. As noted before, Bolivia is an example that stands out as matching your view quite well. Technical work on cadastre and registry are making progress but legal frameworks are remain problematic from the view of capital expansion and financial markets. Yet from other lens – agrarian reform, conflict, indigenous rights, Bolivia has achieved impressive and necessary reform. This history makes the needed reforms in relation to financial markets even more challenging in Bolivia than elsewhere. Guatemala is another example where registry files are electronically modernized but still lack adequate legal reform, consolidation of records to identify

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<sup>3</sup>Not necessarily land titling project advisors – there is likely an ignorance of this issue outside of registry lawyers.

and clean out duplications and other irregularities and there is still a very large percentage of property that is not even covered by the registry. Estimates suggest, notably, that less than 1/3 of formal lending in Guatemala is secured by collateral. There is an active attempt to improve this scenario and more receptivity to reform.

*Besides 'Land Titling:'* Finally, there are other gaps/needs in financial market development that are unrelated to property rights and collateral. These also affect the ability of title to have an impact on credit access. There is a need for specialized financial services that address the peculiarities of agriculture and rural enterprise. Clients must have income and ability to pay. Information on clients must be available in a cost-effective manner. In agriculture, linkages across actors in the 'supply-chain' – inputs (including capital) – production – and product markets – often provide risk mitigation enabling lending without collateral pledges. This is an important example to understand and area for expanded emphasis in the broader discussion.

### **Summary and Conclusions**

In sum, I suggest that a) it is important to continue to build effective property rights systems that serve multiple purposes; b) it is important to work on the complementary elements of the legal framework that enable title to market linkages and to inform the design of information systems from the client perspective; c) it is important not to lose sight of innovative financial product availability with a wide variety of approaches to risk management - including but not limited to lending secured by real property.

It is really too bad we haven't been having this conversation for the last half decade or more. As much as the authors call on the 'land titling' camp to pay more attention to and work toward tackling important issues in the legal and informational framework for secured lending, I put the onus equally on the 'rural finance' camp. It is no more natural that investments in issues that fall in the nexus between property rights and finance be supported within 'land titling' projects than separately or in projects aimed at expanding micro, small and medium enterprise finance. Moreover, in my experience, the emphasis on microenterprise in the last decade, has meant that not many financial market programs designers even wanted to talk about secured transactions. Even among those who were paying attention to secured lending, there was a tendency to mainly look at moveable property. That is because these were viewed as ways around the image of 'politically difficult and technocratically intransigent land titling projects.'

Today, as you look more thoroughly at rural financial market development, that there is an emerging consensus on best practices that answer many of the problems that the authors raise about 'land titling' and using land-use rights as collateral. Between the laundry list I give and the one put forth in the paper having to do with issues unrelated to property, one could be tempted again to shy away from secured lending. The issues are numerous but surmountable. An increasingly broad coalition of interests can achieve – and put into practice – needed legal reforms. I would welcome further opportunity to share with you materials, examples, and contacts so that we might work together at the nexus of two very critical issues areas – finance and property.

Sources of Information (handouts available at the conference based on these).

1. Sanjak, Jolyne (March 2001) “Finanzas Rurales: Derechos de Propiedad y Mercados de Tierras” Presented at IDB Conference on Rural Development, Guatemala City, Guatemala. (www.
2. Sanjak, Jolyne (1999) USAID Concept paper for the Inter-Summit Property Systems Initiative (IPSI) paper and other information on the IPSI web-site ([www.property-registration.org](http://www.property-registration.org), )
3. World Bank Policy Research Review on Land Policy and Land Administration (forthcoming 2003) [www.worldbank.org/landpolicy](http://www.worldbank.org/landpolicy) and background consultations (papers, e-conferences).