

# GRAIN ELEVATOR BANKRUPTCIES: UNDERSTANDING YOUR LEGAL RIGHTS AS A PRODUCER

Grain elevators are similar to other businesses in your community. Most are financially sound, well-managed and efficiently operated. But, with the economic climate that now exists, many businesses, including elevators, are challenged to maintain a healthy business. Adverse basis movements, declining volumes, high interest rates, and shifts in transportation rate structures can inflict heavy financial burdens on well-run elevator operations.

Under such conditions, poor management can result in a financially weak or insolvent elevator. Symptoms may or may not be obvious, such as undercapitalization, speculation in the futures market, kiting (issuing checks without sufficient funds to cover them to raise money or maintain credit temporarily), improper hedging of grain purchased under delayed pricing contracts, and other indicators of poor management.

From July 1, 1983 through June 30, 1985, 108 grain elevators in the U.S. declared bankruptcy. That's not many elevators when you consider the thousands of elevators that dot the rural areas of our nation, but it is more than double the previous two-year period. Losses at these 108 elevators involved millions of bushels of grain, millions of dollars, and hundreds of farmers.

Bankruptcy is a proceeding under federal law whereby the bankruptcy firm either (1) has its assets liquidated, proceeds dispersed and remaining debts cancelled (referred to as Chapter 7) or (2) establishes a court-approved plan to reorganize its business, usually by extending the time period it has to pay its debts as well as being discharged of those it can not pay (referred to as Chapter 11). Insolvency is a state law procedure similar to the first alternative under bankruptcy except the remaining debts are not cancelled. Due to this difference, many debtors prefer federal bankruptcy over state insolvency proceedings.

If you were one of the farmers who dealt with an elevator that declared bankruptcy or experienced insolvency, it may have meant a loss for you. The information here may help you avoid such a situation in the future.

## You Can Protect Yourself

Here are some things to watch for when you consider doing business with any elevator. If you answer **yes** to any of the following questions, investigate the financial condition

of the business and the possibilities of marketing your grain through other elevators.

**1. Does the grain buyer or warehouseman consistently offer prices higher than other buyers in your area without a valid reason for doing so? Some buyers or warehousemen may do this occasionally to increase their volume, increase cash flow and operating money, or to cover commitments already made for the grain.**

**2. Does the buyer or warehouseman offer economic incentives not usually offered in the purchase of grain like little or no discount for high damage, dockage, or moisture?**

**3. Does the buyer or warehouseman have a history of slow payment, issuing bad checks, or recurring financial problems?**

**4. Does the buyer or warehouseman ask you to hold a check for a few days before depositing it or until he receives payment for the grain?**

**5. Does the buyer or warehouseman urge you to leave your grain money on deposit, even promising interest?**

**6. Does the buyer or warehouseman give you an oral promise instead of a written contract?**

**7. Does the buyer or warehouseman try to persuade you not to ask for your stored grain, and does he want to pick up your receipt without paying for it?**

Here are some things you can do to minimize your risk:

**1. Know who you sell to! Learn all about your buyer. Is it a well-established business? How well financed is it? Does the manager run a "business-like" operation? Does the buyer have a fixed facility? Can you reach the buyer at a place of business? What does your bank think of the buyer?**

**2. Demand accurate weights and grade. Settle for a fair price. Don't be greedy - the market will bear only so much. Don't ask a dealer to do something for you that you wouldn't want him to do for others.**

**3. Demand payment for sale grain when due - cash your check promptly.**

4. Don't risk crop after crop. Never let your contracts or moneys due extend beyond one year.

5. Request written documents for all transactions. Read thoroughly. If you don't understand, ask for clarification.

6. Do business only with a licensed and bonded warehouse. Laws require that warehouses meet certain standards and undergo periodic examinations. Most states require elevators that store grain for the public to be licensed and bonded either under state or federal warehouse laws.

Elevators in North Dakota are required to be licensed and bonded for an amount equal to approximately one dollar for each bushel of storage capacity. These bonds benefit persons holding grain warehouse receipts, scale tickets, checks, or other memoranda given as evidence of delivering, storing, or selling grain. State law prescribes that grain which remains unsold 20 days after delivery to an elevator will be considered stored and protected by the bond. Despite this broad coverage, farm operators should request warehouse receipts for all grain they intend to store in an elevator. State law does not require the bond to cover credit-sales which include agreements to sell grain in which the elevator does not pay for the grain within 30 days of its delivery.

7. Understand the risks associated with credit-sales which include delayed pricing and deferred payment contracts. Unless these contracts require payment within 30 days after delivery or release of the grain, the bond will not apply. Ownership of the grain will have transferred to the elevator and you will be considered having extended credit. You will not have the same rights as storage depositors.

Delayed pricing (also known as priced later contract) is when a farmer delivers and sells his grain with an understanding that he will set the price at a future date. Deferred payment is when grain is delivered, priced and sold with an understanding that the farmer will not receive payment until a later date, probably the next tax year. Likewise, a farmer is extending credit when he delivers his grain for immediate sale and pricing without a contract or payment.

If you sell grain to a buyer or warehouseman and agree to any of these arrangements, you are extending credit to the buyer. Ask yourself if you would loan the buyer a like amount of cash without security. When there is any doubt about a credit-sale contract or about getting paid, consider alternative selling arrangements or look for another buyer.

8. In case of bankruptcy (federal law) or insolvency (state law), farmers who have sold their grain but have not been paid will have to wait with other unsecured creditors for their share of the proceeds after the elevator assets are sold and secured creditors are paid. However, farmers who had not sold their grain but were storing it in the elevator are owners of the grain. Any farmer who can prove the grain is his will, with court approval, be able to take possession of it or have a claim against the bond. In case of insolvency of a North Dakota elevator, ownership can be proven with either a warehouse receipt, storage ticket, check, or other memoranda protected by the bond. A credit-sale contract will NOT be accepted as evidence of ownership in case of elevator insolvency. In case of an elevator filing bankruptcy under federal law, "warehouse receipt, scale ticket, or similar document of the type routinely issued as evidence of title...shall constitute evidence of a claim of ownership."

9. Farm operators should not rely exclusively on state bonding requirements to protect them against elevator failures. Collecting on a bond is often a long process. Furthermore, bond proceeds are seldom sufficient to cover all claims because the bond amount (approximately one dollar per bushel of storage capacity) is less than the value of a bushel of grain. Likewise, the criteria for determining the amount of bond (storage capacity) is narrower than the coverage of the bond (stored grain as well as total grain purchases during the preceding 30 days).

## In Summary

You cannot protect yourself completely from elevator bankruptcies, but you can minimize your risk of loss by following good business practices. Investigate the financial condition and reputation of the buyer before selling or storing your grain; demand payment for sold grain, get a warehouse receipt for storage grain, have a written record of all transactions, and enter into a credit-sale contract only if you are willing to accept the risks which come with extending unsecured credit. To minimize the risk of these credit type arrangements, you may wish to ask the elevator to provide some security such as a bond, escrow account or an advance payment.

Elevator bankruptcies can be a concern for farmers. However, the basic ideas of good business apply to all purchasers of agricultural products; know the rules regulating the industry, investigate the financial situation of the purchaser and conduct your affairs in a business-like manner. Any purchaser or debtor can go bankrupt.

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