

## **AGRICULTURAL ISSUES STUDY - BACKGROUND MEMORANDUM**

Section 1 of House Bill No. 1467 (2019) directs the Legislative Management to study agricultural issues in the state, including grain buyers, roving grain buyers, grain brokers, and grain handling facilities under North Dakota Century Code (NDCC) Title 60; and issues related to prepayment for fertilizer, soil amendments, seed, and fuel in situations of insolvency. The study must include a review of the current law, industry practices, and background checks relating to grain buyers, roving grain buyers, grain brokers, and handling facilities and a review of any potential efficiencies that may exist, methods of maintaining financial security during the grain buying process, including consideration of facility operating capital to ensure adequate solvency during licensing, and the process of confidential financial and physical audits. The study also must include a review of the law pertaining to grain handling facility asset lists to determine if changes are required to ensure producers are protected from facility insolvency if an end product is refined and no longer reflects the original product, the indemnity fund under Title 60, and grain handling facility bonding requirements.

### **HOUSE BILL NO. 1467**

#### **Study Directive**

House Bill No. 1467, as introduced, would have removed warehouse companies engaged in the marketing, storage, or handling of agricultural products from the general jurisdiction of the Public Service Commission (PSC). The bill also would have amended numerous provisions of NDCC Title 60 to move the authority over grain buyers, warehousing, deposits, and warehousemen from the PSC to the Agriculture Commissioner. The Senate amended the bill to provide for this study.

#### **Testimony**

The legislative history for House Bill No. 1467 indicates concerns were raised about the number of grain inspectors in the state being reduced from 10 to 1.75 full-time equivalent positions. As a result of this reduction, regulation and oversight of grain has been reduced and quality control issues and other detrimental effects have arisen. Testimony indicated although self-insured indemnity funds paid by farmers provide protection for producers in the state, there needs to be better protection and oversight by the state for farmers.

Testimony indicated of the 373 grain warehouses licensed in North Dakota, 264 are licensed by the state and 109 warehouses are licensed by the United States Department of Agriculture. Warehouses with a federal license also purchase a facility-based grain buyer license from the state under NDCC Section 60-02.1-07. There are 99 roving grain buyers licensed in the state. Roving grain buyers typically do not have brick and mortar locations to store, condition, or move commodities. Interest was expressed in limiting a roving grain buyer's annual grain purchases, and requiring a roving grain buyer provide proof of adequate bonding, a verified line of credit from a financial institution, and adequate assets. The minimum bond for a roving grain buyer is \$50,000, as determined in North Dakota Administrative Code (NDAC) Section 69-07-02-02.1.

Testimony also indicated a need to study cash grain brokers. While brokers commission the sale of grain, there are no statutory provisions for oversight, regulation, or bonding of grain brokers. A broker is a middle man who works with a purchaser, who is sometimes from out of state, and an in-state farmer who has unsold grain.

### **WAREHOUSING AND DEPOSITS LAW**

#### **History**

Until the transfer of authority in Senate Bill No. 2009 (2019), grain licensing and inspection had been a part of the PSC's jurisdiction for over 127 years. The last major change occurred in 2003 with the establishment and implementation of the credit-sale contract indemnity fund under NDCC Chapter 60-10. Before the 2003 legislation claimants who held credit-sale contracts were not eligible to receive any repayment if there was an insolvency.

Public warehouses first were defined in 1891 Session Laws Chapter 126 as all "buildings, elevators or warehouses in this State, erected and operated . . . by any person . . . for the purpose of buying, selling, storing, shipping or handling grain for profit . . ." This law required the proprietor, lessee, or any manager of a public warehouse to file a bond with the Board of Railroad Commissioners--the precursor to the PSC. The bond, which was to be not less than \$5,000 nor more than \$75,000, was to be conditioned upon the faithful performance of duty as public warehousemen and upon compliance with the laws of this state.

The statute set forth the requirements for warehouse receipts, storage receipts, and basic provisions governing insolvency. It further provided anyone who willfully neglected or refused to deliver the full amount of grain or the grade and market value of grain to which a person making proper demand was guilty of larceny. The crime of

larceny, as well as any other violation of the Act, which included cheating and falsely weighing wheat or other agricultural products, was deemed a misdemeanor.

The final section of the statute stated "whereas, an emergency exists in that there is at present no code of intelligible warehouse laws upon the statute books of North Dakota . . . this law shall be in force and effect from and after its passage and approval." A similar statute had been enacted by the Territorial Legislature 4 years earlier. The bonding requirements were; however, lower--not less than \$2,000 nor more than \$50,000.

Current law requires public warehousemen to file with the PSC a bond conditioned for the faithful performance of duties and compliance with the law and which is in a sum not less than \$5,000. That same language is applicable to grain buyers. North Dakota Century Code Section 60-02-01 defines a public warehouse as "any elevator, mill, warehouse, subterminal, grain warehouse, terminal warehouse, or other structure or facility not licensed under the United States Warehouse Act [7 U.S.C. 241-273] in which grain is received for storing, buying, selling, shipping, or processing for compensation." A public warehouseman is defined as "the person operating a public warehouse that is located or doing business within this state, whether or not such owner or operator resides within this state."

A grain warehouse may elect to be licensed by federal or state authorities. The federal government regulates grain warehouses under the United States Warehouse Act which is administered by the United States Department of Agriculture. With respect to a grain warehouse licensed by federal authorities, matters regulated by the Act cannot be regulated by the state. Licensing under the Act is voluntary and may be accomplished by applying and qualifying. A grain warehouse licensed under the Act must meet requirements for sound warehouse operations, i.e., furnish an acceptable bond, maintain a minimum net worth, and pay inspection and licensing fees. In lieu of a bond, a warehouse may file a certificate of participation in and coverage by an indemnity or insurance fund, approved by the Secretary of Agriculture, and established, maintained, and backed by the full faith and credit of the applicable state.

The bond for a state-licensed facility is based on the physical capacity of the facility. A federally licensed entity must have a grain buyer's license and a bond based on volume. The Public Service Commission in NDAC Section 69-07-02-02, provides the amount of a warehouse bond is determined by the total physical capacity identified by the licensee, the length of time the license has been licensed, the licensee's annual grain purchase volume, and the licensee's scale ticket conversion policy. The bond ranges from \$50,000 to \$65,000 for a physical capacity that does not exceed 100,000 bushels depending on the length of time the licensee has been licensed. The bond ranges from \$250,000 to \$325,000 for a physical capacity not exceeding 500,000 bushels. If there is capacity in excess of 500,000 bushels, the bond amount increases by \$56,500 for each additional 25,000 bushels or fraction thereof. Unless the PSC determines an increase is necessary to accomplish the purpose of NDCC Chapter 60-02, the bond of a warehouseman may not exceed \$2 million.

In the case of a grain buyer, the bond is determined by the 3-year rolling average of grain purchased annually in this state by the grain buyer. If the grain buyer purchases less than 100,000 bushels, the bond amount is \$50,000. For each additional 100,000 bushels or fraction thereof, up to 1 million bushels, the bond is raised by \$20,000. For each additional 100,000 bushels or fraction thereof, in excess of 1 million bushels, the bond is raised by an additional \$5,000. If the grain buyer is a new licensee, the 1<sup>st</sup> year's bond is based on the projected purchase volume, and the 2<sup>nd</sup> and 3<sup>rd</sup> years' bonds are based on the average actual volume according to the stated schedule. Unless the PSC determines that an increase is necessary to accomplish the purpose of NDCC Chapter 60-02.1, the bond of a grain buyer may not exceed \$2 million.

Senate Bill No. 2009 transferred all regulatory authority over NDCC Title 60, including grain and seed warehouses, grain buyers, insolvent grain warehousemen, uniform accounting for public elevators and warehouses, public warehouses on railroad rights of way, and credit-sale contract indemnity, from the PSC to the Agriculture Commissioner. The bill created new sections to Chapters 60-02 and 60-02.1 to require applicants for a public warehouse or grain buyer license to provide financial records to the Agriculture Commissioner, upon request, as a condition of licensure and to require the Agriculture Commissioner to maintain the confidentiality of the records. The bill also changed the amounts of an annual or biennial license fee for a public warehouse and the bond amount required by an applicant for a grain buyer license.

## **NORTH DAKOTA CENTURY CODE TITLE 60**

North Dakota Century Code Chapter 60-01 provides the general provisions regarding deposits that apply to Title 60, including definitions. Under Section 60-01-01, a deposit may be voluntary or involuntary and be made for safekeeping or exchange. Section 60-01-01.1 was created by Senate Bill No. 2009, and defines "commissioner" as the Agriculture Commissioner. Sections 60-01-02 through 60-01-08 discuss various definitions related to types of deposits. Sections 60-01-09 through 60-01-28 discuss the duties of a depository, delivery provisions, notice of

adverse claims, wrongful detention of a deposit, indemnity, damages, sale of deposit, negligence, and termination of deposit by payment.

Chapter 60-02 regulates grain and seed warehouses. Section 60-02-01 defines terms applicable to the chapter, including commissioner, credit-sale contract, grain, noncredit-sale contract, public warehouse, public warehouseman, receipts, and receiving station. Section 60-02-03 provides for the powers and duties of the commissioner in regulating grain and seed warehouses. Sections 60-02-05 and 60-02-05.1 determine the procedure for resolving disputes related to grain and grain marketing. Section 60-02-06.1 was created by Senate Bill No. 2009 to require any public warehouse that desires to obtain a license to conduct business in the state to provide financial records to the commissioner upon request, authorize the commissioner to obtain financial records regarding the applicant from outside sources, and information obtained by the commissioner is confidential.

Section 60-02-07 provides the licensing and fee requirements for a public warehouse operating in the state. Section 60-02-09 requires a public warehouseman to file a bond with the commissioner as a condition of licensure. The section also provides for requirements related to the bond, including that a bond must specify the location of the warehouse to be covered by the bond and the bond be at least \$5,000 for any one warehouse.

Sections 60-02-10 and 60-02-10.1 require a public warehouse license to be posted in a conspicuous location in the warehouse and allow the commissioner to revoke or suspend a license for cause upon notice and hearing. Section 60-02-11 requires public warehousemen to issue a uniform scale ticket for each load of grain received to the person from whom the grain is received. The section requires all scale tickets be converted into cash, noncredit-sale contracts, credit-sale contracts, or warehouse receipts within 45 days after the grain is delivered to the warehouse unless the recipient signs a waiver. Sections 60-02-13 through 60-02-16 discuss the form, contents, provisions, and copies of warehouse receipts. Section 60-02-17 contains information regarding warehouse and storage contracts and rates. The section requires a warehouseman to post in the warehouse the fees that will be assessed for receiving, storing, processing, or redelivering grain and the termination date of warehouse receipts.

Section 60-02-19.1 provides the circumstances under which a warehouseman may purchase grain under a credit-sale contract, and the information and requirements that must be included in a credit-sale contract. Section 60-02-22 makes a public warehouseman liable to the owner for the delivery of the kind, grade, quality, and quantity of grain called for by the warehouse receipt. Section 60-02-23 requires public warehousemen to keep a record of all grain received, stored, and shipped. Section 60-02-30 addresses the termination of public grain warehouse storage contracts and the notice required to stakeholders. Section 60-02-42 allows the commissioner to issue a cease and desist order if a warehouse engages in activity or practices contrary to the law or rules.

Chapter 60-02.1 provides for provisions regarding grain buyers. Section 60-02.1-01 defines terms applicable to the chapter, including credit-sale contract, facility-based grain buyer, grain, grain buyer, noncredit-sale contract, receipts, and roving grain buyers. Sections 60-02.1-05 and 60-02.1-05.1 determine the procedure for resolving disputes related to grain and grain marketing. Section 60-02.1-06.1, created by Senate Bill No. 2009, requires any grain buyer that desires to obtain a license to conduct business in the state, to provide financial records to the commissioner upon request, and authorize the commissioner to obtain financial records regarding the applicant from outside sources. The section provides information obtained by the commissioner is confidential.

Section 60-02.1-07 provides the licensing and fee requirements for a grain buyer operating in the state. The annual licensing fee for a facility-based grain buyer is \$400. Section 60-02.1-07.1 provides the licensing and fee requirements for a roving grain buyer operating in the state. The annual licensing fee for a roving grain buyer is \$300. Section 60-02.1-08 requires a grain buyer to file a bond with the commissioner as a condition of licensure. The section also provides for requirements related to the bond and provides the bond must be at least \$10,000. The section allows the commissioner to set the bond amount and increase the bond amount as determined necessary. The section also provides only one bond may be required for any series of facilities owned or operated by a facility based grain buyer.

Section 60-02.1-10 requires a licensed obtained by a facility-based grain buyer be posted in a conspicuous place in the buyer's facility. Section 60-02.1-11 allows the commissioner to revoke or suspend a license for cause upon notice and hearing. Section 60-02.1-12 requires grain buyers to issue a uniform scale ticket for each load of grain received to the person from whom the grain is received. Section 60-02.1-13 provides any person in violation of the chapter is guilty of an infraction.

Section 60-02.1-14 provides the circumstances under which a grain buyer may purchase grain under a credit-sale contract, and the information and requirements that must be included in a credit-sale contract. Section 60-02.1-16 requires grain buyers to keep a record of accounts and memoranda concerning the buyer's dealing as

a grain buyer and provides a grain buyer may be required by the commissioner to make reports of grain purchases as required by rules adopted by the commissioner. Section 60-02.1-17 requires licensed and bonded grain buyers to file monthly reports with the commissioner regarding information required by the commissioner.

Section 60-02.1-28 provides a licensed grain buyer is insolvent when the licensee refuses, neglects, or is unable upon proper written demand, including electronic communication, to make payment for grain purchased or marketed by the licensee or is unable to make redelivery upon proper written demand, including electronic communication. Section 60-02.1-29 requires the commissioner to apply to the district court of Burleigh County for authority to take all action as trustee of the trust in case of insolvency by a grain buyer. Section 60-02.1-30 requires a trust fund be established for the benefit of noncredit-sale contract receiptholders upon the insolvency of a licensee. The section addresses which assets must be held in the trust. Sections 60-02.1-32 and 60-02.1-33 addresses the notice to and remedies of receiptholders and credit-sale contract claimants in case of the insolvency of a licensee. Section 60-02.1-39 allows the commissioner to issue a cease and desist order if a grain buyer engages in activity or practices contrary to the law or rules.

Chapter 60-04 addresses insolvent grain warehousemen. Section 60-04-02 provides a licensee is insolvent when the licensee refuses, neglects, or is unable upon proper written demand, including electronic communication, to make payment for grain purchased or marketed by the licensee or to make redelivery or payment for grain stored. Section 60-04-03 requires the commissioner to apply to the district court of Burleigh County for authority to take all action as trustee of the trust in case of insolvency by a warehouseman. Section 60-04-03.1 requires a trust fund be established for the benefit of noncredit-sale contract receiptholders upon the insolvency of a licensee. Sections 60-04-04 and 60-04-05 address the notice to and remedies of receiptholders and credit-sale contract claimants in case of the insolvency of a licensee. In an insolvency proceeding, the PSC uses the grain on hand and the bond to pay cash and warehouse receipt customers. The bond covers these sales and any extra amount does not go to credit-sales. Farmers with a credit-sale contract are unsecured creditors and may collect through a bankruptcy proceeding or a private action. Insolvency and bankruptcy proceedings are mutually exclusive.

Chapter 60-05 addresses uniform accounting for public elevators and warehouses. Chapter 60-06 addresses public warehouses on railroad rights of way.

Chapter 60-10 provides for credit-sale contract indemnity. Section 60-10-01 requires an assessment at the rate of 0.2 percent to be placed on the value of all grain sold in this state under a credit-sale contract, as provided for in Sections 60-02-19.1 and 60-02.1-14. The licensee purchasing the grain is required to note the assessment on the contract required under Sections 60-02-19.1 and 60-02.1-14 and to deduct the assessment from the purchase price payable to the seller. Section 60-10-02 creates the credit-sale contract indemnity fund in the state treasury.

Section 60-10-03 requires the commissioner to suspend collection of assessments once the indemnity fund reaches a level of \$6 million. The section also requires that collection of assessments resume if the balance of the fund falls below \$3 million. Section 60-10-04 addresses who is eligible for reimbursement from the indemnity fund. Section 60-10-06 provides the amount payable from the fund to an eligible individual may not exceed the lesser of 80 percent of the amount owed to the person under credit-sale contracts, or \$280,000. Section 60-10-07 requires the commissioner to prorate payments if claims for indemnity payments from the fund exceed the balance in the fund.

## **2009-10 LEGISLATIVE STUDY**

Pursuant to House Concurrent Resolution No. 3048 (2009), the 2009-10 interim Agriculture Committee studied the bonding requirements placed on grain warehouses and buyers, including ethanol plants and grain processors, and ways to further reduce the financial risk of participants in the sale, purchase, handling, and processing of grain, including the sale of grain to ethanol plants and processors, the payment for grain by such entities, and whether there exists a need for new or increased bonding and indemnification options to reduce financial risk. The question before the committee was whether the warehouse and grain buyer bonds were sufficient to mitigate the financial risk of those who participate in the sale, purchase, handling, and processing of grain, and, in particular, whether ethanol plants and processors should be viewed in a separate risk category.

The committee recognized the PSC had the regulatory ability to adjust bonding levels and the PSC had the statutory authority to introduce legislation to address licensing and bonding issues. The committee made no recommendation regarding its study.

## INFORMATION REGARDING OTHER STATES GRAIN REGULATION AND INDEMNITY

Thirty-eight states regulate warehouse licensing or grain buyers, or both. Of the 38 states, 35 do so through each state's agriculture departments, including North Dakota following the passage of Senate Bill No. 2009. Only South Dakota, New Mexico, and Nebraska regulate through another state agency.

### Indiana

The Indiana Grain Indemnity Program was established by the 1995 General Assembly to protect farmers in the event of a licensed grain buyer's financial failure. The Indiana Grain Indemnity Fund is voluntarily funded by producers who pay a producer premium equal to 0.2 percent of the price on all marketed grain that is sold in Indiana. The program provides payments to producers that have not requested or received a producer premium refund and are economically damaged by the financial failure of a licensed grain buyer. After the fund reaches \$25 million by June 30 during an active collection period, per Indiana law, the board may not require the collection of additional farmer premiums. However, if the fund drops below \$20 million by May 1 during an active collection period, the board may require the collection of additional farmer premiums. In that case, collections will start at the beginning of the fiscal year (July 1) and must continue until the end of the fiscal year (June 30), even if the fund crosses the \$25 million threshold during that year.

If a licensed grain buyer fails, producers that have not requested or received a premium refund may receive 100 percent payment on storage losses which occur at a licensed warehouse, or 80 percent payment on all other financial losses from grain delivered to a licensed grain buyer. The producer's financial loss for unpriced grain is calculated using the market value of the grain on the licensed grain buyer's last day of business, which may not be the same as the sale price, less certain charges, times either 80 or 100 percent. Since 1996, the Indiana Grain Indemnity Fund has paid producers approximately \$4.2 million involving 12 failures. The most recent failure was in 2016.

Indiana law requires any person or firm be licensed by the Indiana Grain Buyers and Warehouse Licensing Agency if over 50,000 bushels of grain are purchased from producers annually, other than for feeding one's own livestock; deferred pricing or any contracts tied to the futures markets are offered; or open storage or grain bank services are offered. Licensees are required to post their license publicly at their place of business. Indiana allows producers to opt-out of the indemnity fund.

### Minnesota

Minnesota has a grain licensing program that licenses both grain buyers and grain warehouses. The program is designed to help protect grain sellers and depositors from monetary loss if they do not receive payment for grain sold or if grain stored is damaged or lost. Under Minnesota's program, a grain buyer license is required by anyone buying grain in Minnesota with the purpose of reselling the grain or products made from the grain. In addition to a license, a bond must be acquired. Bonds requirements range from \$10,000 to \$150,000 and are based on the dollar amount of the buyers annual grain purchases. A grain buyer must apply for a license for each location the buyer operates unless there are multiple storage facilities within the same city.

A grain buy and store license is required to operate a grain warehouse that stores grain for compensation. Grain warehouses must acquire a grain bond which provides reimbursement to depositors experiencing damage or other grain loss. Bonds range from \$10,000 to \$500,000 for storage licenses. Grain warehouses are required to have two examinations each year. Examiners provide an onsite review including an audit of records and a physical measurement of storage bins and facilities to identify total capacities, shortages in storage, over obligations, open storage accounts, contracts, insurance policies, and safety issues. Minnesota does not have an indemnity fund like North Dakota.

## RELEVANT 2019 LEGISLATION

Senate Bill No. 2346 (2019), as introduced, would have required grain warehouses and grain buyers to provide financial records to the PSC upon request, as a condition to receiving a license. The bill also would have provided that any financial records released to the PSC were confidential and could be only released under certain circumstances.

The bill would have required producers who receive scale tickets for each load of grain delivered to a warehouse to convert the ticket into cash, noncredit-sale contracts, credit-sale contracts, or warehouse receipts within 30 days after the grain was delivered unless certain conditions were met. The bill would have required a producer who failed to convert their scale tickets within the designated time period to be treated as a credit-sale contract claimant in the event the warehouseman became insolvent. Regarding an insolvency of a grain buyer, the bill would have allowed noncredit-sale receipt holders to receive reimbursement of the remaining amount owed from the grain producers

indemnity fund if the trust fund established for the benefit of noncredit-sale receipt holders was insufficient to redeem all claims in full.

The bill also would have amended the assessment amount of all grain sold in the state from 0.2 to 0.1 percent and would have placed the assessment amounts in the grain producers indemnity fund; changed the amount in the fund that triggers a suspension on the collection of the assessments from \$6 million to \$10 million; and amended the amount in the fund that triggers resuming collection of the assessments from \$3 million to \$6 million.

The House adopted the bill to mirror the introduced version of House Bill No. 1467 (2019), with additional amendments to move the authority over grain, grain buyers, warehousing, deposits, and warehousemen from the PSC to the Agriculture Commissioner. The House amendments included changes to the amounts for annual license fees for public warehouses, added the new sections that were in the introduced version of Senate Bill No. 2346 regarding the requirement of providing confidential financial statements as a condition of receiving grain warehouse or grain buyer licensure, added definitions of a "cash grain broker" and a "grain processor," added new sections for a cash grain broker and grain processor license, and changed the minimum amount of the bond required for a grain buyer to obtain a license from \$5,000 to \$10,000. The bill failed to pass the Senate.

Senate Bill No. 2009 (2019), the agency appropriation for the Agriculture Commissioner, was amended by the House to incorporate the amendments to Senate Bill No. 2346 as referenced above. The bill was then further amended for conference committee. The bill amended all references in NDCC Chapters 60-02, 60-02.1, 60-04, 60-05, 60-06, and 60-10 from "commission" and "public service commission" to "commissioner" and "agriculture commissioner;" transferred all regulatory authority over Title 60, including grain and seed warehouses, grain buyers, insolvent grain warehousemen, uniform accounting for public elevators and warehouses, public warehouses on railroad rights of way, and credit-sale contract indemnity, from the PSC to the Agriculture Commissioner; created new sections to Chapters 60-02 and 60-02.1 to require applicants for a public warehouse or grain buyer license to provide financial records to the Agriculture Commissioner, upon request, as a condition of licensure, required the Agriculture Commissioner to maintain the confidentiality of the records; and changed the amounts of an annual or biennial license fee for a public warehouse and the bond amount required by an applicant for a grain buyer license.

### **STUDY APPROACH**

In conducting this study, the committee may wish to receive testimony from the Agriculture Commissioner regarding the transition of authority over grain buyers and warehouses under NDCC Title 60 from the PSC, and issues related to the prepayment for fertilizer, seed, soil amendments, and fuel in the case of insolvencies. The committee also may wish to receive testimony from representatives of commodity groups and producers regarding current industry practices, the indemnity fund, and bonding requirements. The committee may wish to receive testimony from bonding companies and banks regarding background checks of grain buyers, roving grain buyers, and handling facilities during the financial review process. The committee also may consider requesting testimony from the PSC for historical reference data regarding regulation over the provisions of Title 60.