

THE REVISED ILLINOIS GRAIN CODE: GREATER PROTECTION TO FARMERS AND LENDERS IF A GRAIN ELEVATOR FAILS

December 2003, by Donald L. Uchtmann and A. Bryan Endres*

Abstract: *This article describes the protections provided to farmers and lenders by the Illinois Grain Code in the event an Illinois-licensed elevator fails. These protections were changed significantly by Public Act 93-0225, effective July 21, 2003, which amended the Illinois Grain Code to incorporate lessons from the Ty-Walk elevator failure. A checklist of “Good Practices” designed to maximize these protections for farmers is included.*

THE 2003 REVISIONS to the Illinois Grain Code (a) provide more protection to farmers if an Illinois-licensed grain dealer or warehouse fails and (b) create new assessments on sellers of grain and some lenders in order to restore solvency to the Illinois Grain Insurance Fund (“IGIF”). This article describes these protections. A separate, companion article describes the new assessments on farmers and lenders.

http://www.farmdoc.uiuc.edu/legal/selling_products/ALTB_03-01.pdf

When a producer or share landlord (“farmer”) delivers grain to an elevator, what payment assurances does the farmer have if the elevator fails? What if a lender has taken warehouse receipts for grain stored at a failed elevator as collateral for a loan? The 2001 failure of Ty-Walk Liquid Sales, Inc. (“Ty-Walk”), based in Minooka, Illinois, revealed that the collapse of a major grain elevator could leave many farmers and lenders with significant, uncovered losses, in spite of protections afforded by the Illinois Grain Code. Public Act 93-0225, effective July 21, 2003, significantly changed the Illinois Grain Code to reflect lessons learned from the Ty-Walk failure. This article describes the current IGIF protection afforded farmers and lenders under the amended Illinois Grain Code.

Overview: Warehouses & Grain Dealers

When grain elevators *store* grain for a farmer, the elevator is acting as a *warehouse*. The farmer may have a “warehouse receipt” as evidence that the elevator is storing the farmer’s grain, or at least scale tickets indicating the grain is to be stored. Lenders may also accept warehouse receipts as security for loans made to the elevator. This warehouse function – storing grain – is regulated by the state or federal government, depending on whether the warehouse has a state or federal warehouse license. Most elevators in Illinois are licensed by the Illinois Department of

Agriculture and subject to the requirements of the Illinois Grain Code.

When an elevator *buys* grain from a farmer, it is acting as a *grain dealer*. This grain dealer function – buying grain – has traditionally been regulated by the states. For example, most Illinois grain dealers are regulated by the Illinois Department of Agriculture under provisions of the Illinois Grain Code and have an Illinois Grain Dealers License. (There are ongoing discussions regarding the future role of the US Department of Agriculture in regulating the grain buying and selling activities of federally licensed grain warehouses, but these discussions are beyond the scope of this article.)

Farmers typically sell grain to an elevator under any of three arrangements. Under the first, the farmer sells grain for the current price. The farmer receives the check as soon as the business office can process the transaction. This arrangement can be described as an “immediate payment sale.”

Under the second arrangement, the farmer delivers the grain to the elevator at the current price, but the contract for sale does not call for payment until a future date (perhaps after the start of the farmer’s new tax year). This arrangement can be described as a “deferred payment sale.”

The third arrangement is where the farmer sells the grain under a “price later” contract, also known as “deferred pricing” or “delayed pricing.” Under the “price later” contract, ownership of the grain passes to the elevator at the time of delivery, but the price to be received by the farmer is determined at a future date with payment made at a later date.

If a grain elevator holding an Illinois Grain Dealer License fails, the IGIF is available, in most circumstances, to assure payment to farmers who

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stored and/or sold grain to the elevator. In addition, the IGIF provides payment assurance to lenders holding warehouse receipts for grain stored in the failed elevator. In both cases, the IGIF is “tapped” to the extent that the grain and equity assets of the failed elevator are insufficient to fund the payment of warehouse and grain dealer claims guaranteed by the act. However, as described below, the payments guaranteed by the Illinois Grain Code will not necessarily cover all the losses incurred by farmers and lenders.

Claims under the Illinois Grain Code

In the Ty-Walk failure, payments under the Illinois Grain Code to claimants totaled approximately \$32 million. Despite the relatively large payout, much of which came from the IGIF, ineligible claims totaled approximately \$14 million – nearly \$4 million in unpaid claims to farmers and nearly \$10 million to lenders. In return for the imposition of new assessments (described in a separate article) farmers now receive increased protection from the IGIF if an Illinois-licensed elevator fails. A brief discussion of the different claims and their limitations follows.

A. Warehouse Claims

Claims concerning losses for grain stored at a failed elevator are known as warehouse claims. Warehouse claims can be submitted by farmers with stored grain, and by lenders that hold warehouse receipts as security for loans. In the event of a grain elevator failure, warehouse claims will be paid up to 100%. A claimant’s pro rata share of the proceeds from liquidating the elevator’s grain assets is first applied against the claim. If the liquidation proceeds fail to fully compensate all warehouse claimants, each claimant is entitled to payment from the IGIF. Payments from the IGIF for warehouse claims, however, are capped at \$1 million per claimant.

B. Farmers’ Grain Dealer Claims

Claims submitted by unpaid farmer-sellers of grain are known as grain dealer claims. Payments from the IGIF for grain dealer claims are capped at \$1 million per claimant (\$250,000 in some cases). A farmer, however, may recover separately up to \$1 million for farmer’s warehouse claims and up to \$1 million for farmer’s grain dealer claims. However, a deferral in receiving payment (a “deferred payment” sale) or a delay in pricing the grain (a “price later” sale) may lower the maximum recovery for a farmer’s grain dealer claims to only \$250,000. Subject to these overall caps, valid claims for some losses are covered at 100% of the loss while others are covered at only 85% of the loss. A brief discussion of the most pertinent rules follows.

1. 21-Day Rule: 100% Guaranteed Payment Up To \$1,000,000

The IGIF guarantees 100% payment of the claim, up to \$1 million, so long as the farmer completed delivery of the grain *and* agreed on a price within 21 days of the elevator’s failure. Therefore, to ensure 100% coverage for up to \$1 million in sales to a grain dealer, farmers must collect within 21 days of delivering *and* pricing the grain for sale.

Example A: On Oct. 1, 2003, Farmer A delivers to Elevator 100,000 bushels of corn and, on the same day, agrees to a price of \$2 per bushel. On Oct. 18, 2003, when Farmer A is still unpaid, the Elevator fails. Farmer A is entitled to full payment of the \$200,000 grain dealer claim because (a) the delivery occurred within 21 days of the date of failure and (b) the grain was priced before the day of failure. In fact, Farmer could have sold (delivered and priced) corn and beans for up to \$1,000,000 and still been fully protected so long as the elevator failure occurred within 21 days of the delivery and pricing.

2. 21- to 160-Day Rule for Deferred Payment Sales: 85% Guaranteed Up To \$250,000

21- to 160-day Rule for Deferred Payment Sales: If payment is delayed beyond 21 days of delivering *and* pricing the grain, but less than 160 days, the farmer is entitled to only 85% of the amount of the claim, up to a maximum payment from the IGIF of \$250,000. (The 2003 amendments to the Illinois Grain Code increase this cap from \$100,000 to \$250,000, and also clarified how the 160 day rule is applied). Therefore, to ensure at least 85% coverage for up to \$250,000 in sales to a grain dealer, farmers must collect within 160 days of delivering and pricing the grain.

Example B: Same as *Example A* except that Farmer and Elevator have agreed that the \$200,000 payment is due January 2, 2004 and the elevator fails on October 29, 2004. Because delivery and pricing of the grain (10/1/03) occurred more than 21 days before Elevator’s failure (10/29/03), Farmer B is not entitled to 100% payment for the \$200,000 loss; however, since delivery of the priced grain occurred within the 160 day period before Elevator’s failure, Farmer B is guaranteed 85% of the \$200,000 loss, i.e., \$170,000. (But if Farmer B had sold corn for \$300,000 under these circumstances, farmer’s guaranteed payment from the IGIF would be capped at \$250,000, not \$255,000 which is 85% of \$300,000).

Example C: On October 1, 2003 Farmer C delivers to Elevator 100,000 bushels of corn and, on the same day, agrees to a price of \$2 per bushel. Farmer agrees to delay payment until July 1, 2004. On May 31, 2004 the

Elevator fails. Because both delivery and pricing of the grain occurred more than 160 days before the failure of the elevator, there is no recovery for Farmer C.

3. 160-Day Rule & 365-Day Rule for “Price Later” sales: 85% Guaranteed Payment Up To \$250,000

160-day Rule for “Price Later” Sales: Where *either* completion of delivery *or* the date of pricing is within 160 days of the elevator’s failure, farmers who file valid claims are also guaranteed 85% of the amount of the claim, up to a cap of \$250,000 per claimant (so long as the 365-day rule is not violated – see below). The date of completion of delivery means the date of the last delivery of grain that was to be applied to the contract’s quantity requirement. (The 2003 amendments to the Illinois Grain Code clarified the way in which this 160 day rule is applied).

365-day Rule for “Price Later” Sales: Either the date of the actual execution of the contract *or* delivery of the grain must be no more than 365 days before the date of failure. (The 2003 amendments extended the maximum period of protection for price later sales from 270 days to 365 days).

If the final price of the grain has not yet been established at the time of failure, the Department will determine the per bushel value of these claims from the average cash bid prices on the date of the failure from grain dealers in the area and cash bid price of the failed grain dealer, less transportation, handling and applicable discounts as of the date of failure.

The execution of subsequent price later contracts by a farmer and grain elevator for grain previously covered by a price later contract will not extend the coverage of an IGIF claim beyond the original 365 day period. Therefore, in order to ensure at least 85% coverage on “price later” grain sales, farmers must collect within 365 days of either delivering the grain or entering into the priced later contract, *and* within 160 days of delivering or pricing the grain.

Example D: On September 1, 2003, Farmer D and Elevator enter into a “price later” contract for 20,000 bushels of beans. Farmer completes delivery of the 20,000 bushels on November 1, 2003. On March 1, 2004, Elevator fails. Because the grain was delivered (11/1/03) within 160 days of Elevator’s failure (3/1/04), Farmer is entitled to 85% of the value of the grain *as of the date of failure* (grain was not priced at time of failure), subject to a maximum payment from the IGIF of \$250,000. Farmer D will recover 85% of \$140,000 (i.e., \$119,000) assuming the price of beans on 3/1/04 was \$7.00/bu. (If Elevator had failed on 5/1/04 and Farmer had still not priced the grain,

Farmer D would not be protected by the IGIF because neither delivery nor pricing had occurred within 160 days of the failure.)

Example E: On September 1, 2003, Farmer E and Elevator enter into a “price later” contract for 20,000 bushels of beans. Farmer completes delivery of the 20,000 bushels on November 1, 2003. On July 1, 2004, Farmer and Elevator agree on a price of \$7 per bushel with payment to be made on January 1, 2005. On August 1, 2004 the elevator fails. Because the grain was priced within 160 days of Elevator’s failure, Farmer E is entitled to 85% of the amount owed, subject to a maximum payment from the IGIF of \$250,000. Farmer E will recover \$119,000 (85% of 20,000 bu. x \$7/bu. price-later price). (Note: If the Elevator had failed on November 5, Farmer would not be protected by the IGIF because both the date of the contract (9/1/03) and delivery (11/1/03) would be more than 365 days before the elevator failure (11/5/04).

4. \$250,000 Cap Is on Farmer’s Combined Claims for Deferred Payment and Price Later Sales

Where a farmer has claims for both deferred payment and price later sales, the maximum payment from the IGIF for the combined claims is \$250,000.

Example F: In the preceding examples Farmers B, D, and E received, respectively, \$170,000 (85% of a deferred payment sale), \$119,000 (85% of a price later sale), and \$119,000 (85% of a price later sale) from the IGIF (each subject to the \$250,000 payment limit per claimant). If the same claims had been filed by one claimant, Farmer F, then Farmer F’s recovery from the IGIF would be capped at \$250,000.

Increased Oversight of “Farmer Marketing” Programs, Other Marketing Services

Elevators offering various marketing services with “higher risk” will be subject to more comprehensive annual examinations. Ty-Walk’s “farmer marketing” programs contributed to its failure in 2001. Based on this experience, the 2003 amendments to the Illinois Grain Code clarify and expand the responsibilities of the Illinois Department of Agriculture regarding oversight of “farmer marketing programs” and other “higher risk” marketing services offered by some elevators. The level of risk associated with the licensee’s grain merchandizing and trade practices will determine the scope of the annual exam by the department. The intent is that the increased oversight of licensees will provide greater protection to farmers and lenders by reducing the likelihood of elevator failure.

Farmer “Good Practices” to Maximize Protection under the Illinois Grain Code

- √ Do not store grain worth more than \$1 million at any one licensed warehouse (the maximum recovery available from the IGIF for “Warehouse Claims” is \$1,000,000 per claimant).
- √ To assure 100% coverage for up to \$1 million in sales of grain to a Grain Dealer, always collect within 21 days of delivering and pricing the grain for sale (if you delay payment beyond 21 days but not more than 160 days, you are only entitled to 85% of the sale proceeds if the elevator fails, or \$250,000, whichever is less).
- √ To assure at least 85% coverage on grain sales for which the price has been determined, but payment has been delayed more than 21 days:
 - never let more than 160 days pass before collecting, and
 - never let the amount owed to you by any one licensee for such delayed payment sales (plus amounts owed for price later sales) exceed \$250,000.
- √ To assure at least 85% coverage on “price later” grain sales
 - always collect ► within 160 days of the later of delivering or pricing the grain, and ► within 365 days of the later of delivering the grain or entering into the price later contract
 - never let the uncollected value of such price later sales (plus amounts owed for delayed payment sales) to any one licensee exceed \$250,000.
- √ Understand the risks and benefits associated with “farmer marketing programs” or other “higher risk” services offered by licensees (loses from trading activity are not covered by the IGIF).



Conclusion

The 2003 revisions to the Illinois Grain Code generally provide more protection to farmers if an Illinois-licensed grain dealer or warehouse fails. The amendments increased from \$100,000 to \$250,000 the caps on certain payments of grain dealer claims. In addition, the revised statute extends protection for Price Later contracts from 270 to 365 days, and clarifies the responsibilities of the IL Department of Agriculture to oversee “higher risk” marketing services provided by elevators. This increased protection, however, comes at a price as farmers and lenders are now subject to direct assessments designed to replenish the Illinois Grain Insurance Fund. These new assessments and the increase in size of the IGIF are discussed in a separate, companion article.

The complete language (unofficial) of the revised Illinois Grain Code is available on the Internet. Go to <http://www.legis.state.il.us/legislation/ilcs/ilcs.asp> and CLICK on “CHAPTER 240 WAREHOUSES.” Then CLICK on “240 ILCS 40/ Grain Code.”

Updates of this article will also be available on the *farmdoc* Website, in the Law and Taxation section (see <http://www.farmdoc.uiuc.edu/legal/index.html>).

DISCLAIMER: This article by Uchtmann and Endres is designed to help farmers gain a basic understanding of the possible claims allowed under the Illinois Grain Insurance Fund. Although the authors try to ensure the accuracy of this information, they cannot guarantee that all the information is accurate or current. Laws change quickly and the reader should always ensure that any legal information is up-to-date and accurate before relying on it. Moreover, the statute described above may contain additional detailed requirements and limitations beyond the scope of this article and this statute is subject to additional interpretation or clarification by the Illinois Department of Agriculture. The information contained in this article is for educational purposes only.