

# Enhancing Protection for Stored Grain at Public Grain Warehouses

*FINAL REPORT OF THE  
GRAIN WAREHOUSE TASK FORCE*

Submitted to  
Texas Department of Agriculture

November 22, 2010



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## **GRAIN WAREHOUSE TASK FORCE MEMBERS**

Ben Boerner – Texas Grain & Feed Association

Tom Engelke – Texas Agricultural Cooperative Council

Brian McCuiston – South Texas Country Elevator Association

George Caldwell – Texas Farm Bureau

David Gibson – Corn Producers Association of Texas

Rodney Mosier – Texas Wheat Producers Association

Wayne Cleveland – Texas Grain Sorghum Association

Jeff Nunley – South Texas Cotton and Grain Association

Web Wallace – Cotton and Grain Producers of Lower Rio Grande Valley

Ronnie Gerrik – Blackland Cotton and Grain Producers Association

Dale Swinburn, Tulia, TX – Producer

Robert Fleming, Troy, TX – Producer

Dale Murden, Monte Alto, TX – Producer

Ed Small – Jackson Walker L.L.P.

George Ferguson – Frank Bailey Grain

Jim Johnson – First Victoria National Bank

Josh Winegarner – Texas Cattle Feeders

## **EXECUTIVE SUMMARY**

Commissioner Todd Staples appointed a Grain Warehouse Task Force on April 23, 2010, to provide input and recommendations to the Texas Department of Agriculture (TDA) related to grain warehouse regulation. In 2009, more than five grain warehouses filed bankruptcy or experienced failure, directly affecting grain deposited by producers and other depositors. Producers and industry have expressed concern about the current protections provided in law for grain deposits and are interested in finding ways to improve these protections.

The goal set forth for the task forth was to identify workable measures for the regulated industry while also enhancing protection for stored grain. The objectives were as follows:

- 1) Review existing grain warehouse laws and the regulatory framework.
- 2) Develop recommendations to enhance oversight and regulatory functions associated with grain warehouses.
- 3) Develop recommendations for legislative changes to increase protections for grain depositors.

The Grain Warehouse Task Force met on April 27, May 19, June 30, and October 13, 2010 to review current practices, regulations, and laws administered by TDA in the grain warehouse program. Meetings were held in Austin, Texas as well as via conference call. The Task Force assembled subcommittees to focus on specific issues and each subcommittee provided recommendations for discussion and consensus building within the Task Force. On November 1, 2010, the Task Force met in Austin to finalize the recommendations and a report to the Commissioner of Agriculture. The recommendations agreed upon by the Task Force are provided in this report as well as proposed changes to the Texas Administrative Code, Chapter 13 (regulations) and Texas Agriculture Code, Chapter 14 (statute).

## **TASK FORCE SUBCOMMITTEES**

On May 19, 2010, the Grain Warehouse Task Force organized the following three subcommittees: Financial Requirements/Reporting, Bonding Requirements/Bonding Alternatives, and Statute/Regulations. The charge for each subcommittee was to discuss issues associated with the subcommittee focus area and provide recommendations back to the overall Task Force for final review and consensus building of the recommendations. The following sections provide additional information about each subcommittee, their membership, and recommendations developed.

### **Financial Requirements/Reporting Subcommittee**

The Financial Requirements/Reporting Subcommittee met on June 2, 2010 to develop recommendations related to the financial requirements used by TDA as well as to develop financial reporting requirements for public grain warehouses. Members of the subcommittee included Brian McCuiston, Jim Johnson, Tom Engelke, and Jeff Nunley. The subcommittee developed a recommendation for a three-tiered risk rating system to evaluate the financial solvency of a grain warehouse. The ratings are as follows: 1-acceptable; 2-mid-range/ok; and 3-

borderline/insolvent. The system would assign ratings based on an average of the liquidity and leverage for a particular grain warehouse. Liquidity is a measure of a company's solvency and can be determined by dividing current assets by current liabilities, resulting in a current ratio (CR). A tier 1 rating would have a CR of 1.5 or higher; a tier 2 rating would have a CR of 1.0 - 1.49; and a tier 3 rating would be less than 1.0. Leverage is determined by dividing total liabilities by total capital. For leverage, a tier 1 rating would have a ratio of 1.0 or less; a tier 2 rating would have a ratio of 1.1 – 2.99; and a tier 3 rating would be 3.0 or higher. The average rating using liquidity and leverage would then be used for specifying the quality and frequency of financial reporting, based upon annual grain sales.

The reporting requirements identified in the system specified that a warehouse with a tier 1 rating may submit either a compiled financial statement (i.e., TDA form RGW-306), a reviewed financial statement, or an audited financial statement, depending upon annual grain sales. For warehouses with a tier 2 or tier 3 rating, the system specified either a reviewed or an audited financial statement.

Discussion within the Task Force on the recommended three-tiered risk rating system lead to the review of departmental files to identify the types of financial reporting provided by warehouses that were insolvent. The data indicated that six of eight grain warehouses experiencing failure between 2004 – 2009, submitted a compiled financial statement TDA form RGW-306. The Task Force recommended that only a reviewed or audited financial statement be accepted in the future to meet financial reporting requirements.

### **Bonding Requirements/Bonding Alternatives Subcommittee**

The Bonding Requirements/Bonding Alternatives Subcommittee met on June 22, August 11, and August 24, 2010 and also discussed recommendations via email correspondence. Members of the subcommittee included David Gibson, George Caldwell, George Ferguson, and Wayne Cleveland.

The subcommittee discussed the use of the compiled financial statement TDA form RGW-306 and supported the recommendation that TDA require the submission of either a reviewed or audited financial statement for financial reporting requirements. The subcommittee reviewed the current bonding requirements and discussed how an increase in the bond amount would impact grain warehouse operators. Changes to the bonding amount included an increase from six cents to ten cents per bushel of storage capacity, in combination with an increase in the minimum bond amount from \$20,000 to \$35,000. It was further recommended to establish a maximum bond amount of \$500,000, similar to federal warehouse requirements.

A review of TDA grain warehouse files revealed that 69 warehouse operators would be impacted by an increase in the minimum bond amount from \$20,000 to \$35,000. The subcommittee agreed to the recommended changes to the bonding rate and minimum bond amount. After further discussion on establishing a bond maximum, it was further recommended to set a bond amount of ten cents per bushel for temporary storage capacity, with no maximum bond amount. A final recommendation of establishing a minimum net worth requirement of \$200,000 was discussed. A review of TDA grain warehouse files revealed that 18 warehouse operators would be impacted

by the establishment of a \$200,000 minimum net worth requirement. The subcommittee reached consensus in support of this recommendation as well.

### **Statute/Regulations Subcommittee**

The Statute/Regulations Subcommittee met on August 30 and October 29, 2010 as well as conducted a review of the laws and regulations via email correspondence. Members of the subcommittee included Ed Small, Ben Boerner, and Rodney Mosier. In developing recommended changes to Texas Administrative Code, Chapter 13 and Texas Agriculture Code, Chapter 14, the subcommittee mostly reviewed recommendations provided by other Task Force subcommittees and by TDA staff. Recommendations for changes to Texas Administrative Code, Chapter 13 (regulations) and Texas Agriculture Code, Chapter 14 (statute) were provided during the November 1, 2010 Task Force meeting. After review and discussion of the draft changes, additional changes were included in the drafts and the finalized versions of each document can be found in the appendix of this report.

### **RECOMMENDATIONS**

The Grain Warehouse Task Force developed and reached consensus on the following recommendations:

1. Implement a Three-Tier Risk Rating System to evaluate the financial solvency of a grain warehouse. Ratios for liquidity and leverage would be used in the system to specifying the quality and frequency of financial reporting.
2. Eliminate the use of the compiled financial statement TDA form RGW-306 and require the submission of either a reviewed or audited financial statement for financial reporting requirements.
3. Increase the bond amount from six cents to ten cents per bushel of storage capacity, for grain stored in a public grain warehouse.
4. Increase the minimum bond amount from \$20,000 to \$35,000.
5. Establish a maximum bond amount of \$500,000, for grain stored in a public grain warehouse.
6. Require a bond amount of ten cents per bushel for temporary storage capacity, with no maximum bond amount.
7. Establish a minimum net worth requirement of \$200,000.
8. Clarify and/or eliminate certain terminology used in Texas Administrative Code, Chapter 13.

9. Allow a change in a daily position report from stored grain to company owned when supported by a proof of payment, instead of the current requirement of a canceled check.
10. Establish that the price of a grain commodity, when calculating the amount of a claim on a bond, is set when a warehouse operator's license is suspended by the department.
11. Modify the confidential business information requirements in Texas Agriculture Code, Chapter 14, to clarify when certain information and the type of information for a grain warehouse that may be released to the public and law enforcement agencies.
12. Establish that the department may suspend a license if a shortage of grain is discovered or if the warehouse operator refuses inspection.
13. Remove the number of days the department may suspend a grain warehouse license during a licensing period and provide the warehouse operator the ability to lift the suspension by filing a court action.

The Task Force discussed the following issues but did not develop a recommendation:

1. Establishment of an indemnity fund for producers for recovery of losses on stored grain resulting from a shortage.
2. Establishment of a licensing and regulatory structure for grain dealers.

# **APPENDICES**

## RECOMMENDED CHANGES

### Texas Administrative Code Chapter 13. Grain Warehouse

#### 13.2 General Requirements

In addition to any other obligations set out in the Texas Agriculture Code (the code), Chapter 14, Subchapter A, or these rules, the warehouse operator shall be responsible for the general obligations of this section. In the event of a conflict between these general obligations and the obligations established elsewhere, the code shall control first and then the most specific provision which provides the greatest protection to the depositor or other customer of the warehouse. These responsibilities are in addition to any provided in the code.

(1)-(6) (No change).

(7) The daily position report shall declare all grain in the warehouse or in temporary storage as either receipted grain, open storage grain including terminal, or company-owned grain including terminal storage. Company owned grain may be reported paid and unpaid, separately or combined in the daily position report. Any change on the daily position report shall be supported by at least one of the following documents:

(A) a signed copy of the contract of purchase. Such contract shall not be part of any scale weight ticket, settlement agreement, or other unrelated document issued by the licensee;

(B) proof of payment [~~a canceled check~~];

(C) a canceled grain warehouse receipt; or

(D) a scale weight ticket.

(8) –(14) (No change).

(15) Records must have a legend, code sheet, or key list showing the meaning of any abbreviations or headings in main record keeping system sufficient to allow inspection of the records without further interpretation by warehouse operator, authorized agent, or other employee.

(16) Records must be legible, correct, and accurate~~[and able to be understood without asking the warehouse operator, authorized agent or other employee].~~

(17)-(18) (No change).

### 13.6 Financial Statements

(a) A warehouse operator shall submit a financial statement showing the net worth of the operator as part of the operator's application for a new license and thereafter shall submit a new financial statement, reflecting the operator's net worth at the end of the operator's most recent fiscal year, no later than the 90<sup>th</sup> day following the end of the operator's most recent fiscal year ~~[A notarized financial statement must be submitted on a department-approved form unless it is submitted by an independent certified public accountant].~~

(b) Through March 31, 2011, the financial statement required by subsection (a) must be notarized and on the most current version of department form RGW-306 Financial Statement, unless the statement is a reviewed or audited financial statement prepared and signed by an independent certified public accountant. Effective April 1, 2011, the financial statement required by subsection (a) must be a reviewed or audited financial statement prepared and signed by an independent certified public accountant ~~[A warehouse operator has 90 days from the end of the operator's fiscal year to submit a new financial statement to the department].~~

(c) If the department has reason to believe that the financial status of the warehouse operator has changed significantly since the last financial statement was submitted or if the department becomes aware of inaccurate or false information within or information omitted from a submitted financial statement, the department may by written notice require the operator to provide additional financial information and in the case of inaccurate, false, or omitted information may require the operator to submit a new or updated audited financial statement prepared and signed by an independent certified public accountant [The most current financial statement shall be on file at the time of license renewal. A license will not be issued or renewed if the warehouse operator fails to file the most current new financial statement by May 31].

(d) The notice required by subsection (c) shall state the reasons why the department believes the financial status of the warehouse operator has significantly changed or specify the information the department believes is inaccurate, false, or omitted, as applicable. An operator's disagreement with the information set forth in the notice required by subsection (c), however, shall not operate to excuse the warehouse operator from complying with the notice [For a partnership, all assets subject to suit must be included in the financial statement].

~~[(e) For a corporation, all assets subject to suit must be included in the financial statement. No private assets can be included in this case.]~~

~~[(f) For a sole proprietor, all assets subject to suit must be included.]~~

(e-g) Temporary storage shall be included in determining net worth bonding requirements and additional net worth bonding may be required before a temporary storage permit is issued [must meet all financial requirements before a temporary permit may be issued].

### 13.7 Fees

(a)-(b) (No change).

~~[(e) Proration of fees. Initial application fees shall be prorated based on the remaining months of the license year.]~~

(c [d]) Inspection fees. The fee for an annual inspection is \$15.00 for each 10,000 bushels or a fraction of 10,000 bushels of the licensed storage capacity, or \$100.00, whichever is greater.

(e [f]) Requested inspections.

(1)-(3) (No change).

### 13.14 Temporary Storage

(a)-(f) (No change).

(g) A temporary permit for temporary storage grain is valid ~~good~~ for 90 days and may be renewed if the department determines that quality of grain has not been affected by weather conditions.

(h)- (i) (No change).

(j) At any time the warehouse operator determines that more temporary storage is needed, he will have 10 days from the date the amount exceeded the temporary license to file ~~turn in~~ additional bonding and insurance.

(k)-(m) (No change).

### 13.15 Shortage of Grain

(a)-(f) (No change).

~~[(g) If a shortage is corrected by payment with a check that is tendered for cashing within 30 days of its receipt by the depositor, the shortage will be considered not corrected if the check is returned to the depositor for insufficient funds.]~~

### 13.16 Customer Protection

(a) (No change).

(b) Documentation of charges at time of payment or invoicing shall be individually indicated ~~down~~ for each individual charge.

(c) (No change).

### 13.18 Depositor Claims on Warehouse Operator's Bond

(a) For the purpose of calculating the amount of a claim on a bond, the price of a grain commodity is set when a warehouse operator's license is suspended by the department for a shortage of grain~~[Time at which claim amount becomes fixed is the day on which the claim was submitted to the department]~~.

(b)-(c) (No change).

# RECOMMENDED CHANGES

## AGRICULTURE CODE

### TITLE 2. DEPARTMENT OF AGRICULTURE

#### CHAPTER 14. REGULATION OF PUBLIC GRAIN WAREHOUSE OPERATORS

##### SUBCHAPTER B. GENERAL PROVISIONS

Sec. 14.012. BUSINESS INFORMATION. (a) Except as provided in subsection (b), financial information of a warehouse operator provided to the department [~~The following information, prepared by the department in the course of its regulatory authority under this chapter or required to be submitted to the department in accordance with the department's administration of this chapter,~~] is confidential and not subject to public disclosure:

[~~(1) inspection or investigation reports containing information regarding grain inventory; and~~]

[~~(2) financial information provided to the department to establish net worth for purposes of licensing.~~]

(b) Notwithstanding subsection [~~Subsection~~] (a), [~~inspection reports containing information regarding grain inventory of a warehouse operator or~~] financial information of a warehouse operator provided to the department [~~to establish net worth~~] may be disclosed:

(1) [~~entered into evidence without sealing and made public in:~~]

[~~(A)~~] without sealing in an administrative proceeding commenced by the department against a warehouse operator;

~~[(B)] [a civil or criminal proceeding commenced by]~~ (2) to a local or state law enforcement officer, a county attorney, a district attorney, or the attorney general, acting either independently or on behalf of the department, investigating the ~~[against a]~~ warehouse operator;  
or

~~[(C)]~~ (3) in a civil proceeding commenced by the warehouse operator against the department;

(4) in response to a subpoena from a party in a civil proceeding commenced against the warehouse operator.

~~[(2) provided]~~ (5) to the issuer of a warehouse operator's bond or letter of credit~~[for the purpose of establishing a claim on the warehouse operator's bond or letter of credit];~~

~~[(3) disclosed]~~ (6) to the public after:

(A) revocation of a warehouse operator's license;

(B) a voluntary closeout of all of the license holder's facilities in this state;

(C) a petition for bankruptcy has been filed; or

(D) a receiver ~~[is appointed]~~ for the warehouse operator's assets; or

~~[(4) disclosed]~~ (7) to any federal agency or any agency of another state conducting a compliance inspection or criminal or civil investigation involving the handling, storing, shipping, selling, purchasing, or receipt of grain.

(c)For the purpose of this section “financial information” means:

(1) a financial statement or other document provided by the warehouse operator to the department to evaluate net worth requirements under section 14.031 (e) of this chapter;

(2) a financial audit provided by the warehouse operator to the department;

(3) the price of grain paid by the warehouse operator to a depositor or other seller of grain delivered to or stored or handled by the warehouse operator; and

(4) the price of grain paid by or to the warehouse operator by a depositor or other purchaser of grain delivered to or stored or handled by the warehouse operator; and

(5) the terms of payment for a price described by paragraphs (3) and (4) of this subsection.

(d) Notwithstanding any other provisions of this section;

(1) a party to a contract or other agreement with a warehouse operator may obtain a non-redacted copy of the contract or agreement; and

(2) a person who authored or contributed to the creation of financial information may be provided access to the financial information for the purpose of confirming the authenticity, truthfulness, or accuracy of the information.

#### SUBCHAPTER D. BONDING

Sec. 14.031. BOND. (a)-(c) (No change).

(d) The bond must be in an amount of not less than \$35,000 [~~\$20,000~~] and be based on ten [~~six~~] cents per bushel of storage capacity, up to a maximum of \$500,000. The bond amount for temporary storage is ten cents per bushel of temporary storage capacity, with no maximum bond amount.

(e) If the actual net worth of an applicant equals less than the greater amount of either 25 cents per bushel of storage capacity or \$200,000, the applicant shall file a deficiency bond in an amount equal to the difference between the actual net worth and the greater amount of either \$200,000 or the [~~an~~] amount determined by multiplying 25 cents times each bushel of storage

capacity in the applicant's warehouse. A deficiency bond is in addition to the bond required of an applicant by this section.

(f)-(j) (No change).

#### SUBCHAPTER G. REMEDIES AND CLAIMS

Sec. 14.066. APPEAL OF DEPARTMENT ACTION BY WAREHOUSE OPERATOR. (a) A department action or order affecting a warehouse operator under this chapter~~[, other than by rulemaking, assessment of an administrative penalty, or imposition of a license sanction, including a suspension under Section 14.083(e),]~~ is appealable in accordance with this section, unless the action involves agency rulemaking, the assessment of an administrative penalty, imposition of a license sanction, or any other action for which a specific administrative or judicial remedy is available under this chapter, Chapter 12 of this code, or Chapter 2001 of the Government Code.

(b)-(c) (No change).

#### SUBCHAPTER I. ENFORCEMENT

Sec. 14.082. DISCOVERY OF SHORTAGE; REFUSAL OF INSPECTION. (a) If the department determines that a warehouse operator does not possess sufficient grain to cover outstanding receipts and outstanding scale weight tickets issued or assumed by the warehouse operator, or if a warehouse operator refuses or is unable to submit records or property for lawful inspection or the department is unable to conduct an inspection of the warehouse due to the condition of the warehouse or grain stored in the warehouse, the department may seal the warehouse to prevent delivery or receipt of grain except as authorized by the department,

suspend the license of the warehouse operator, and give notice to the warehouse operator requiring the warehouse operator to submit records or property for lawful inspection, to correct any condition interfering with the department's inspection of the warehouse or grain, or to cover a shortage of a particular type of grain by:

(1) storing to the credit of or delivering to each depositor affected by the shortage grain of the same type and quality that is stored at any of the warehouse operator's licensed warehouses in this state and that has been designated as company-owned grain by the warehouse operator;

(2) purchasing and storing to the credit of or delivering to each depositor affected by the shortage grain of the same type and quality;

(3) selling company-owned grain of a different type and paying to each depositor affected by the shortage, on a pro rata basis, the market value of the depositor's grain as determined on the day the shortage was discovered by the department; or

(4) using any combination of the remedies described by Subdivisions (1)-(3) or another fair and reasonable method for meeting the shortage approved by the department.

(b)-(e) (No change).

(f) A suspension issued under this section remains in effect until lifted by the department through written notice to the warehouse operator or as provided by Section 14.066 of this chapter. ~~[At any time before the 11th day following the day on which the department takes possession of grain under this section, the warehouse operator may serve notice on the department to appear in the district court of the county in which the public grain warehouse is located to show cause why possession should not be restored to the warehouse operator. The~~

~~court shall fix the time of the hearing not less than 5 nor more than 15 days from the date of service of the notice.]~~

Sec. 14.083. DENIAL, REVOCATION, MODIFICATION, OR SUSPENSION OF LICENSE OR PROBATION. (a)-(b) (No change).

(c) ~~[H]~~ In addition to or in lieu of a suspension authorized by another provision of this chapter, if the department considers it necessary, the department may suspend a license and prohibit the movement of grain into or out of a warehouse without a hearing for up to 30 days [for one or more periods not to cumulatively exceed 30 days in one licensing period]. For good cause, a suspension under this subsection may be extended for additional periods of up to 30 days each not to cumulatively exceed 90 days in a licensing period.

(d)-(e) (No change).

(f) A suspension issued under subsection (c) of this section remains in effect until lifted by the department through written notice to the warehouse operator or as provided by Section 14.066 of this chapter or it expires by operation of law in accordance with the department's notice of suspension or the limitations set forth in subsection (c).



## **GRAIN WAREHOUSE TASK FORCE CONFERENCE CALL**

Date: Tuesday, April 27, 2010  
Time: 8:00 - 10:00 a.m.

Dial-in Number: (866) 410-9327  
Code: 9475541101

### **Agenda**

- I. Introductions
- II. Task Force Goals and Objectives
- III. Member Input - Identify Regulatory Framework Topics/Areas for Discussion at Future Meetings
- IV. Set Tentative Date and Time for Next Meeting

## **GRAIN WAREHOUSE TASK FORCE CONFERENCE CALL NOTES**

Date: Tuesday, April 27, 2010

Time: 8:00 - 10:00 a.m.

### **I. Introductions**

Task Force members attending:

Ben Boerner, George Caldwell, Wayne Cleveland, Tommy Engelke, George Ferguson, Robert Fleming, Ronnie Gerrik, David Gibson, Jim Johnson, Brian McCuistion, Rodney Mosier, Dale Murden, Jeff Nunley, Ed Small, Dale Swinburn, and Web Wallace.

TDA staff attending: David Kostroun, Rick Garza, Brian Murray, David Gipson, Lance Williams, and Kerry Cowlshaw.

Recommendation: refrain from using specific names for a particular grain warehouse.

### **II. Task Force Goals and Objectives**

Gather input, identify topics/areas of interest. Develop workable measures. Enhance producer protection.

### **III. Member Input - Identify Regulatory Framework Topics/Areas for Discussion at Future Meetings**

- Areas identified by members for future discussion/focus:
  - a. Indemnity fund/insurance policy
  - b. Internet banking related solution
  - c. Definite payment requirements
  - d. Issues related to working capital capacity limitations
  - e. Examine factors that led to failures
  - f. Focus on financial and net worth requirements
  - g. Education for producers on grain warehouse requirements and required information
  - h. Difference in federal and state grain warehouse programs.
  - i. Focus – target audit/inspections on high risk/problem areas.
  - j. Overview of laws and regulations
  - k. Overview of TDA processes
  - l. Review 30-day suspension requirement

### **IV. Set Tentative Date and Time for Next Meeting Wednesday, May 19, 2010**



## **GRAIN WAREHOUSE TASK FORCE MEETING**

Date: Wednesday May 19, 2010  
Time: 9:00 a.m. - 4 p.m.  
Location: Robert E Johnson (REJ) Bldg., 1501 North Congress, Austin  
North Conference Room

### **Agenda**

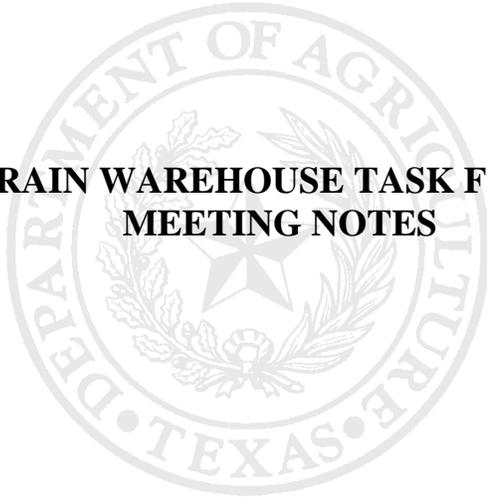
#### Morning Session

- I. Welcome – Commissioner Staples
- II. Grain Warehouse Program Processes and Procedures Presentation – Rick Garza
  - a. Laws and Regulations
    - Overview
    - Questions and Answers/Open Discussion
  - b. TDA Grain Warehouse Program Processes
    - Licensing
    - Inspection
    - Questions and Answers/Open Discussion

#### LUNCH BREAK

#### Afternoon Session

- III. Indemnity Funds (IF)
  - Review Of IF Operation In Other States (Conference call participants from Idaho, Iowa, North Dakota, and Ohio.)
  - Open Discussion/Recommendations
- IV. USDA Grain Warehouse Program
  - Comparison Of Federal vs. State Program
  - Open Discussion/Recommendations
- V. Risk Based Inspection (RBI) – David Kostroun
  - Concepts of RBI/Developing Risk-Factors
  - Open Discussion/Recommendations
- VI. Wrap Up



**GRAIN WAREHOUSE TASK FORCE  
MEETING NOTES**

Date: Wednesday May 19, 2010  
Time: 9:00 a.m. - 4 p.m.

**I. Welcome**

Commissioner Staples welcomed the group and reinforced the importance of the goals and objectives for the task force.

Task Force Members present: Ben Boerner, Brian McCuistion, David Gibson, Ed Small, George Caldwell, George Ferguson, Jeff Nunley, Jim Johnson, Josh Winegarner, Rodney Mosier, Ronnie Gerik, and Tommy Engelke.

TDA Staff present: David Kostroun, Brian Murray, David Gipson, Catherine Wright Steele, Rick Garza, and Kerry Cowlshaw.

Others in attendance: Sara Haines, office of Representative Larry Phillips.

**II. Grain Warehouse Program Processes and Procedures Presentation**

Rick Garza provided an overview of the TDA grain warehouse law, regulations and program processes.

Definitions in Chapter 14 (law): Ed Small suggests that the definition for depositor and other definitions need to be reviewed and clarified.

TDA allows for correction of a noncompliance (such as a shortage) within a specified time period. Suggestion was made that TDA immediately impose restrictions when a facility is found short of grain (i.e., immediately stop grain movement out of the facility).

**III. USDA Grain Warehouse Program**

A conference call was held with USDA Federal Grain Warehouse Program: Patricia Barrett and Tim Meil:

The federal program has a licensing agreement:

- Qualifications
- Financial requirement to qualify
- Bonding
- Duties of Warehouse operation
- Receipts
- Service License – weigher checks & facility
- Determination of Quality
- Temporary/emergency license
- Dispute resolution
- Fines/Penalties

Financial Requirements:

- Warehouse Act requires \$200,000 net worth
- Financial statement must be audit level or review level by third party
- Can grant 30-day extension to get financial statement

USDA starts with the balance sheet. They back out certain items from the statement and figure financial requirement. Ask for explanation on removed items. If short on net worth, provide options: Infusion of capital, Letter of Credit, Bond

Provide 3 to 3-1/2 weeks to respond. Can work with a warehouse to get into compliance.

Do allow an interim financial statement to update a previously submitted statement.

USDA reviews notes of financial statements. The third party audits will list any significant events.

Must meet 1:1 ratio on working capital. Current assets to current liabilities, if not 1:1, allow warehouse to correct.

Require depreciable and fixed assets and inventory to be insured.

Use book value (can use appraised values but must have certification appraisal).

Make sure scales are up-to-date, building is in good condition and operator is knowledgeable of operating a warehouse.

Take appraisal value minus book value and allow 70% to be used for net worth.

Tax appraisal records are not allowed.

Land can use appraisals from realtors but no improvements – must be a certified appraisal.

USDA asks for accounts receivable aging and will back out an aging accounts receivable.

Federal inspectors do not look at financials, but they do look at insurance. Sometimes they find uninsured inventory (grain).

Note: Grain warehouses do a monthly report to their insurance company.

Change in Daily Position report (DPR) - Provide source documents for DPR (list of receipts, open storage) and test source documents to ensure included in DPR.

USDA bond requirement: Maximum \$500K per state.

In the Fed system, if a check is issued to move grain from open storage to company-owned, the evidence required is that the check was written, unlike the state system where a canceled check is required as evidence to move grain to a company owned position.

#### IV. **Risk Based Inspection (RBI)**

David Kostroun led a discussion on a risk-based inspection concept.

Risk is defined as the combination of probability and consequence (impact). The highest risk is mostly associated with a small percentage of locations.

Risk based inspection (RBI) uses risk factors rather than the traditional time-based approach. RBI permits allocating inspection and maintenance resources to provide a higher level of coverage on the high-risk locations and an appropriate effort on the lower-risk locations.

The group discussed considering size/risk of an operation for submission of a DPR on a quarterly basis.

Ben Boerner suggested that if electronic reporting is implemented, it may take less time and could mean reduced fees. This is how you entice the industry.

Suggestion that if a warehouse has financial problems, put reporting requirements in place.

The group was supportive of a risk-based inspection concept.

#### V. **Indemnity Fund Discussion**

A conference call was held with state grain warehouse officials in Idaho, Iowa, North Dakota and Ohio, concerning the use of an indemnity fund in their state.

Each state talked about how their program functioned. Most states have a cap on their indemnity fund and most states met the cap in the past and are not currently collecting fees.

Ben Boerner posed some questions and concerns about a fund after the call: Why not hear from Kansas since they do not have an indemnity fund? We are not a grain origination state; we have a large amount of grain that comes into the state. Interested in seeing how Illinois and Indiana handled with significant losses.

## VI. **Wrap Up**

General discussion occurred prior to meeting adjournment.

Suggestion that audited/reviewed financial statements will bring credibility to the system. Getting payable/receivables aging reports are needed to assess working capital.

In order to facilitate review of key areas of focus from the meeting, three subcommittees were developed, with TDA staff assigned as a resource. The groups will meet and bring recommendations back to the overall task force for discussion and final recommendations.

### **Statute/Regulations**

Ed Small  
Rodney Mosier  
Ben Boerner  
David Gipson (TDA)

### **Bonding Requirements/Bonding Alternatives**

David Gibson  
George Caldwell  
George Ferguson  
Wayne Cleveland  
Lance Williams/Brian Murray (TDA)

### **Financial Requirements/Reporting**

Brian McCustion  
Jim Johnson  
Tom Engelkey  
Jeff Nunley  
Rick Garza (TDA)

Next Meeting: Tentatively scheduled for June 14, 2010.  
(MEETING CHANGED TO CONFERENCE CALL – TO BE HELD JUNE 30, 2010)



**GRAIN WAREHOUSE TASK FORCE  
CONFERENCE CALL**

Date: Wednesday June 30, 2010

Time: 8:30 - 10:30 a.m.

**Agenda**

- I. Introduction of Call Participants
- II. Report out: Financial Requirements/Reporting Committee – Brian McCuiston
- III. Discussion
- IV. Status of Progress by Other Committees

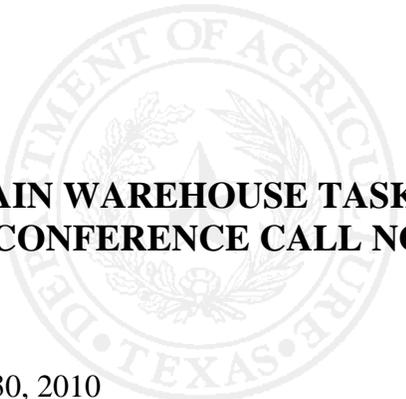
To connect to call:

Toll Free Dial in Number: 866-556-1189 or

Toll Dial in Number: 210-406-8205

Participant Code: 5213595

If you have last-minute problems, call Kerry at 512-517-6283.



**GRAIN WAREHOUSE TASK FORCE  
CONFERENCE CALL NOTES**

Date: Wednesday June 30, 2010

Time: 8:30 - 10:30 a.m.

**I. Introduction of Call Participants**

Task Force Members present: Brian McCuiston, David Gibson, Ed Small, George Caldwell, George Ferguson, Jeff Nunley, Jim Johnson, Robert Fleming, Rodney Mosier, Ronnie Gerik, Tom Engelke, and Wayne Cleveland.

Texas Department of Agriculture staff present: David Kostroun, Brian Murray, Joe Benavides, Rick Garza, David Gipson, Lance Williams, and Kerry Cowlshaw.

**II. Report out: Financial Requirements/Reporting Committee – Brian McCuiston**

On behalf of the group, reported that the sub-committee, including Brian, Jim Johnson, Tom Engelke, Jeff Nunley, and Rick Garza met. He provided the Recommendations and Conclusions document that came from their meeting, for discussion as a basis to begin from in developing financial requirements.

From Financial Assessment, apply rating of 1, 2, or 3. 1-acceptable; 2-midrange-ok; and 3, borderline/insolvent.

3-Tier Risk Rating based on 2 factors – liquidity and leverage. Annual sales considered a more efficient measure than capacity.

Liquidity is a measure of a company's solvency and can be determined by dividing current assets by current liabilities = "Current Ratio" (CR). Tier 1 would have a CR of 1.5x or higher; Tier 2 CR of 1.0x-1.49x; and Tier 3 is less than 1.0. Anything less than

1 is a problem. There could be temporary periods of time when a warehouse may fall below 1 but if below 1 for a year, this would justify more scrutiny.

Leverage determined by Total Liability divided by Total Capital.

Overall Rating – average of Liquidity and Leverage Rating.

Quality and Frequency of Financial Reporting dependent on Annual \$s in Grain Sales (AGS) and Overall Rating. Annual Sales defined as: \$0-10 mm, \$10-20 m, and \$20m+. A 3 Rating would have increased Monthly or Quarterly Reporting.

### III. Discussion

Discussion determined that for Ratings 1 and 2, a Reviewed FS would suffice for all levels of AGS.

Discussion included that a facility would be able to include factors like seasonal influences and market fluctuations in review with Arbitration Committee (review by peers). Setting a “1 and below” as in “watch” category. Watch category could include financial reporting frequency and TDA licensing requirement. Currently, belief is that 60-75% of facilities will fall in 1 to 1.5 ratio. Intention to not punish GWs in stable financial status.

Request was made to evaluate facilities with recent failures inside the proposed Risk Assessment and report back to the full committee. That will be done and sent to the all members.

Rating frequency – if in place would it catch previous failures? Can catch if going downhill; if committing fraud, may not always be able to identify.

Questioning rating – in 2 and 3 Ratings, would this result in increased TDA inspections? Although that was not addressed, comment was made that yes, inspection frequency should increase.

Comment that new examiner position should have agriculture background to understand industry and how it works. TDA noted that USDA has offered to do training with whoever is hired.

Costs Associated to do an Audited statement – one member indicated approximately \$20,000; Reviewed – approximately half or slightly less than an audited statement. Cost is impacted by the quality of internal controls and record keeping done at facility. Too big a job for single person to audit across the entire state. Question raised about types of financial statements provided in recent failures. Rick Garza pulled files and reported that 4 failures provided TDA form RGW-306 Financial Statement; each statement indicated viable financial net worth.

Difference between Audit and Review financial statements. Jim Johnson provided brief overview of distinction. Audited – CPA attests to validity of report. Reviewed statement is interim report; CPA, using Generally Accepted Accounting Principles has a variety of checks and balances in place – not as inclusive or extensive as Audited report.

Question – current bu capacity in Texas...Rick provided ~233m bu state licensed. Costs of statements: 7m bu between \$14-15,000 for audited and Reviews ~1/2 that price or less. Brian McCuiston estimated that the cost of an audit was approximately ¼ cent per bu.

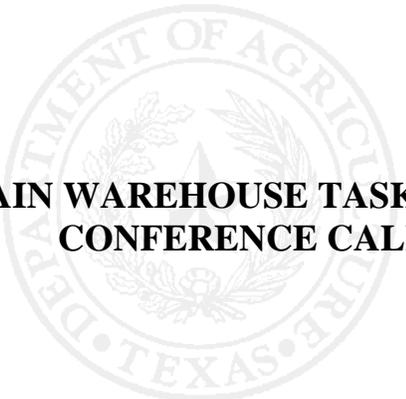
Jim Johnson pointed out that TDA has had limited resources. Future – analyst will be utilized. Current regulations contain authority to review financial records. Self-reporting net worth uniformly thought by members to not be as reliable as Reviewed statements. Mom and pop size concern raised about financial impact of requiring an Audited or Reviewed statement. Minimum recommendation was to provide Review statement. Comment made to not place anything more onerous than what USDA already has in place. Recommendation to look at 2 years average financial status before changing reporting requirements or risk, due to weather factors and bunching of grain sales.

Jim Johnson indicated that most banks will require an audited statement to finance a large facility.

**IV. Status of Progress by Other Committees**

The Bonding/Bonding Alternatives Group met recently. No recommendations from that group yet. Questions raised had been answered and will be supplied when Rick reports out on ratings for previously failed facilities.

Conclusion – meeting notes will be prepared and sent after other info is assembled. Meetings in the near future will be held via conference call; when recommendations have been developed, then meet at a location to be determined to formalize those recommendations.



**GRAIN WAREHOUSE TASK FORCE  
CONFERENCE CALL**

Date: Wednesday October 13, 2010

Time: 11:00 a.m.

**Agenda**

- I. Roll Call of Participants
- II. Report out/discussion: Bonding and Bonding Alternatives Sub-committee – George Ferguson
- III. Status of Progress – Laws/Regulations Sub-committee
- IV. Update on Discussion Related to Establishment of Indemnity Fund – David Gibson and George Caldwell
- V. Finalize Task Force Meeting Date and Agenda (to be held in Austin)

To connect to call:

Toll Free Dial in Number: 866-759-8351 or

Toll Dial in Number: 210-339-2032

Participant Code: 1650028

If you have last-minute problems, call Kerry at 512-517-6283.



## GRAIN WAREHOUSE TASK FORCE CONFERENCE CALL NOTES

Date: Wednesday October 13, 2010

Time: 11:00 a.m.

### **I. Introduction of Call Participants**

Task Force Members present: Ben Boerner, Brian McCuiston, Dale Murden, David Gibson, Ed Small, George Ferguson, Jeff Nunley, Ronnie Gerik, and Web Wallace. Texas Department of Agriculture staff present: David Kostroun, Brian Murray, Kelly Book, Joe Benavides, David Gipson, Rick Garza, Lance Williams, and Kerry Cowlshaw.

### **II. Report out/discussion: Bonding and Bonding Alternatives Sub-committee**

Recommendations are made to move bonding amount from .06 per to .10 a bushel, increase the bonding minimum from \$20,000 to \$35,000, and to require either a reviewed or audited financial statement, removing the option to self-report. Still under consideration is a change to the minimum net worth based on capacity. Some discussion considered increasing the minimum. This change would impact only smaller facilities. To spread across all licensees, an increase to the .25 per bushel capacity net worth requirement would be needed. Discussion was opened to the full committee for comment; there were no comments or opposition.

### **III. Update on Discussion Related to Establishment of Indemnity Fund – David Gibson and George Caldwell**

The Task Force has no consensus on investigating an indemnity fund. Several groups, separate from the Task Force, were represented at a recent meeting held to discuss an indemnity fund. David Gibson explained that proposals are being refined and visits with end users and grain handlers are being done. He provided reassurance that information will, with interest from Task Force members, be presented to the Sub-committees and to the entire Task Force. David Kostroun was asked if TDA was in favor of or pushing for an indemnity fund. David informed the group that TDA is neutral.

### **IV. Status of Progress – Laws/Regulations Sub-committee**

The committee is waiting on recommendations from the Bonding and Bonding Requirements sub-committee. Areas identified so far where changes to statute or law area needed include: requiring reviewed/audited financial statements, bond amounts,

and risk-based inspection criteria. Ed Small commented that statutory authority is needed to allow TDA to move faster and more decisively. The current system leaves protection grain buyers out through the lengthy time period to move through a failure. If grain buyers are left out, the system breaks down.

Ben Boerner noted that the timetable of when things were in good shape and then fall apart may indicate timer periods too long or short and no teeth, using Circleville and Murphy as examples. The 30-day suspension is not enough; may need ability to automatically extend based on need.

**V. Finalize Task Force Meeting Date and Agenda (to be held in Austin)**

The full committee discussed dates and determined Nov. 1 as an option. The group will be contacted through email.



## GRAIN WAREHOUSE TASK FORCE

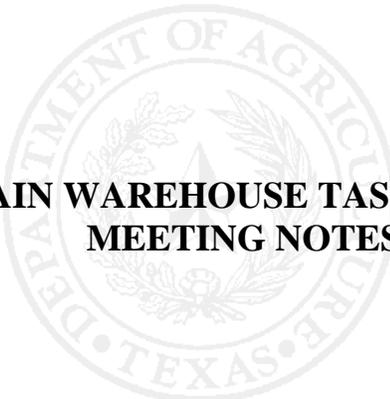
Date: Monday, November 1, 2010

Time: 9:00 a.m.

Location: Stephen F. Austin Bldg.  
Enter and check in with security, through east entrance off Congress Avenue  
1700 North Congress, Austin, TX 78711  
10<sup>th</sup> Floor, Room 1003A – RED Conference Room

### Agenda

- I. Welcome and Introductions – David Kostroun
- II. Overview of Agenda and Goals of the Meeting – David Kostroun
- III. Update from Bonding and Bonding Alternatives Subcommittee – Rick Garza
- IV. Update from Producer Grain Committee on Indemnity Fund – Scott Frazier and Dee Vaughan
- V. Review Recommendations from Laws and Regulations Subcommittee – TBD
- VI. Wrap-up of Recommendations / Draft Legislative Changes and Plan for Task Force Report to Commissioner Staples – David Kostroun



## GRAIN WAREHOUSE TASK FORCE MEETING NOTES

Date: Monday November 1, 2010

Time: 9:00 a.m.

Location: Stephen F. Austin Bldg.  
1700 North Congress, Austin, TX 78711  
10<sup>th</sup> Floor, Room 1003A – RED Conference Room

### I. **Welcome and Introductions**

David Kostroun welcomed the group and introductions were made. Task Force

Members present: Ben Boerner, Brian McCuistion, David Gibson, Ed Small, George Caldwell, George Ferguson, Jeff Nunley, Jim Johnson, Josh Winegarner, Rodney Mosier, Ronnie Gerik, Tommy Engelke, Wayne Cleveland, and Web Wallace.

Guests: Dee Vaughan, Texas Corn Producers; Ken Hodges, Texas Farm Bureau; Scott Frazier, Texas Farm Bureau; Sara Haenes, Representative Larry Phillips staff; and Troy Skarke, Texas Grain Sorghum Board.

Texas Department of Agriculture staff attending: David Gipson, David Kostroun, Joe Benavides, Kelly Book, Kerry Cowlshaw, Lance Williams, Mike Mann, and Rick Garza.

### II. **Overview of Agenda and Goals of the Meeting**

David Kostroun gave a brief overview of the agenda and the goals of the meeting. A question was raised about the focus of the task force and general discussion took place regarding the task force goals, authority needed by the department, reasons for grain warehouse failures, and other discussion about how proposed recommendations and the TDA grain warehouse examiner position might increase protection against warehouse failures.

**III. Update from Bonding and Bonding Alternatives Subcommittee**

Rick Garza reported on two additional recommendations from the Bonding and Bonding Alternatives subcommittee. A maximum bond amount of \$500,000 was proposed, with temporary storage remaining at ten cents per bushel of storage capacity and no maximum bond amount. Also proposed was the enactment of a minimum net worth requirement of \$200,000. Discussion included discovery that 17 state licensed elevators would be affected by the \$200,000 minimum net worth requirement. Consensus was reached to accept the recommendations.

**IV. Update from Producer Grain Committee on Indemnity Fund – Scott Frazier and Dee Vaughan**

Scott Frazier and Dee Vaughan gave a presentation to the Task Force on a grain indemnity fund proposal, developed by grain commodity groups and Texas Farm Bureau. The importance of producer protection was outlined, with emphasis that if the producer does not survive, other businesses would also fail. A draft document was provided to task force members and after a brief overview of the proposal, a question and answer session was held.

It was emphasized that producers would pay into the fund and fee collection/coverage would be at first point of sale of grain. Grain dealers/merchants would be required to license with TDA. It was proposed that TDA would administer the fund. It was noted that program was proposed to be mandatory.

After discussion about the fund, the Task Force decided against the development of a recommendation concerning the establishment of an indemnity fund.

**V. Review Recommendations from Laws and Regulations Subcommittee**

Rick Garza raised a question about whether to consider assets of a parent company in the event of a large conglomerate. The Task Force determined that assets would be considered only if held in the same name as the licensee.

Concern was raised about grain warehouses being shut down but continuing to buy and sell grain. It was mentioned that a grain dealer law may address that issue. After a brief discussion on this issue, the Task Force decided against the development of a recommendation concerning a grain dealer law.

The Task Force reviewed recommendations presented by the Laws and Regulations Subcommittee. All recommendations were accepted and additional suggestions were provided for clarification and clean-up of language in the Texas Administrative Code as well as slight modifications in proposed wording in the Texas Agriculture Code. The changes will be incorporated and a revised draft sent to members.

**VI. Wrap-up of Recommendations / Draft Legislative Changes and Plan for Task Force Report to Commissioner Staples**

David Kostroun thanked the Task Force for all their hard work. He indicated that the recommendations/draft laws and regulations will be updated and sent to members for review. A draft report will also be sent to members for review and the goal is to submit the final report of the task force to Commissioner Staples no later than December 1, 2010.

The meeting was then adjourned.