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BILL



ANALYSIS

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Senate Bills 1396 and 1397 (as reported without amendment)
Sponsor: Senator Gerald Van Woerkom
Committee: Agriculture and Bioeconomy

Date Completed: 7-7-10

RATIONALE

Two Michigan statutes are designed to protect producers of "farm produce" (corn, soybeans, dry edible beans, cereal grains, and small grain) from the financial failure or fraud of grain dealers. The Grain Dealers Act, enacted in 1939, requires a person to obtain a license from the Michigan Department of Agriculture (MDA) in order to engage in the business of buying, exchanging, selling, or storing farm produce. Grain dealers also must give the MDA a surety bond or other security to secure the performance of their obligations. The Farm Produce Insurance Act, enacted in 2003, established the Farm Produce Insurance Fund to reimburse farm producers for losses incurred when a grain dealer fails or is unable to pay a claim after the farmers have delivered produce to the dealer. Participating farmers must pay into the Fund a premium of up to 0.2% of the net proceeds from all produce sold to a licensed grain dealer, although that payment has been suspended since 2008 when the Fund balance reached its statutory ceiling of \$5.0 million.

Several issues have come up since the Fund began receiving money in 2005. Although the Farm Produce Insurance Act allocates up to \$250,000 to the MDA annually for administrative purposes, that distribution evidently is not adequate to cover the Department's costs of inspecting grain elevators, where produce is stored. In addition, since the Fund covers the risk of a grain dealer's failure, some people believe that a surety bond is no longer needed from grain dealers who store farm produce. In addition, it has been suggested that the

MDA should be able to adjust the license fee annually, rather than every three years as currently allowed, to reflect changes in the consumer price index. The board that controls the Fund also has recommended additional revisions, including clarification regarding producers' eligibility for reimbursement from the Fund.

CONTENT

Senate Bill 1396 would amend the Grain Dealers Act to permit the Michigan Department of Agriculture to adjust grain dealers' fees annually, rather than every three years. The bill also would repeal a section of the Act that requires a grain dealer (except a grain merchandiser or farm produce trucker) to provide a surety bond.

Senate Bill 1397 would amend the Farm Produce Insurance Act to do the following:

- **Permit the Farm Produce Insurance Fund to be used to reimburse the MDA Director for administering and enforcing the Grain Dealers Act, and increase the maximum allocation to the MDA to \$500,000.**
- **Require the board of the Farm Produce Insurance Authority to enter into a memorandum of understanding with the MDA Director to provide for that reimbursement.**
- **Describe circumstances under which a producer would not be eligible for reimbursement from the Fund.**

- **Permit the board to determine the distribution of money in the Fund if the Farm Produce Insurance Act were held invalid.**
- **Permit the board to select the certified public accountant to conduct the annual audit required under the Act.**

The bills are described in detail below.

Senate Bill 1396

Grain Dealers' Fees

The Grain Dealers Act prohibits a person from acting or offering to act as a grain dealer in the State without a license from the MDA. ("Grain dealer" means a person engaged in the business of receiving, buying, exchanging, selling, or storing farm produce in this State, with certain exceptions. The term includes a farm produce trucker, a grain merchandiser, and a processor, i.e., a person who processes farm produce and stores it for more than 24 hours.)

A grain dealer must pay a license fee to the MDA with an application for a license or license renewal. The current fee is the sum of the amounts shown in Table 1, as applicable:

Table 1

For each receiving point with a total bushel capacity of:	
1 - 100,000	\$158
100,001 - 200,000	\$236
200,001 - 300,000	\$315
300,001 - 400,000	\$394
400,001 or more	\$473
For vehicles owned by a farm producer trucker:	
One vehicle	\$210
Each additional vehicle	\$105
For a grain merchandiser's license	\$473

The grain dealer's fee must be deposited into the Grain Dealer's Fees Fund, to be used by the MDA Director to carry out duties required by law. The bill specifies that the MDA would be the administrator of the Fund for auditing purposes.

The Act authorizes the MDA to adjust the fee schedule every three years by an amount determined by the State Treasurer to reflect the cumulative annual percentage change in the Detroit consumer price index (CPI) over that three-year period. The adjustment may not exceed 5%, and must be rounded to the nearest whole dollar.

The bill would permit the MDA to adjust the fee every year to reflect the annual percentage change in the Detroit CPI over that period, not to exceed 5%. The fee would have to be rounded to the nearest \$5 increment.

Repeal of Surety Bond Requirement

The bill would repeal Section 27 of the Act. Under that section, before a license is issued to a grain dealer (other than a grain merchandiser or farm produce trucker), the grain dealer must give the MDA a bond that secures the dealer's warehouse receipts and open storage transactions. (Section 28 of the Act establishes surety bond requirements for grain merchandisers and farm produce truckers.)

The amount of the bond under Section 27 must be \$15,000 for the first 10,000 bushels of storage capacity and \$5,000 for each additional 10,000-bushel capacity or fraction of that capacity. A grain dealer who owns two or more facilities may furnish separate bonds for each facility or a blanket bond. A blanket bond must be for the cumulative amount described above for each facility or \$400,000, whichever is less.

In lieu of a bond, a grain dealer may give the MDA a certificate of deposit or other security acceptable to the Department.

Senate Bill 1397

Producer Security Activities

The Farm Produce Insurance Act established the Farm Produce Insurance Fund to reimburse farm producers for losses incurred if a grain dealer fails or is unable to pay a claim after the producers have delivered produce to the dealer. Participating producers must pay into the Fund a premium of up to 0.2% of the net proceeds from all produce sold to a licensed grain dealer (a licensee) in the State, until the Fund has received \$5.0 million in premiums.

The Fund is under the direction and control of the board of directors of the Farm Produce Insurance Authority, which must direct payments from the Fund to pay only the following:

- Valid claims.
- Producer premium refunds.
- Administrative expenses.
- Legal fees and legal expenses.

Under the bill, the board also could direct payments from the Fund to reimburse the MDA Director for producer security activities.

"Producer security activities" would mean any action by the MDA Director under Section 22 of the Grain Dealers Act to administer or enforce that Act. (That section prescribes the powers and duties of the Director, including the authority to audit and investigate the receipt, storage, processing, buying, selling, and handling of farm produce, and complaints related to those activities.)

The bill would require the board of directors of the Authority to enter into a memorandum of understanding with the MDA Director that provided for reimbursing the Director from the Fund for producer security activities.

The Farm Produce Insurance Act requires the board to allocate money from the Fund to a separate administrative expenses account. That allocation may not exceed \$250,000 each fiscal year. The bill would increase the maximum allocation to \$500,000 and would require that account to be used to reimburse the Director for producer security expenses as well as administrative expenses.

Eligibility for Reimbursement

The Act allows a producer to submit a claim for reimbursement from the Fund if the producer satisfies one of the conditions in the Act related to a licensed grain dealer's failure, and the producer has not previously requested a refund or previously received a refund and reentered the program as prescribed by the Act. (The Act allows a producer to receive a refund of premiums paid to the Fund; the producer then is not entitled to participate in the program or receive a payment under the Act. The

producer may reenter the program by paying previously refunded premiums.)

Under the bill, a producer would be ineligible for reimbursement if the claim related to delivery of farm produce to a licensee that was a cooperative association, under an agreement between the producer and the licensee that allocated delivery rights and obligations proportionate to a capital investment of the producer in the licensee.

("Cooperative association" would mean that term as defined in 12 USC 1141j, i.e., any association in which farmers act together in processing, preparing for market, handling, and/or marketing their farm products, or any association in which farmers act together in purchasing, testing, grading, processing, distributing, and/or furnishing farm supplies and/or farm business services, provided that the association is operated for the mutual benefit of the members and meets certain other requirements.)

A producer also would not be eligible for reimbursement if, at the time the claim was submitted, excluding patronage interests, the producer owned at least 5% of the voting shares, other than publicly traded shares, membership interests, partnership interests, or other ownership interests, of the licensee whose failure was the basis of the claim. ("Patronage interests" would mean shares or membership, partnership, or other ownership interests in a licensee that is cooperative association that are allocated and distributed to the producer in proportion to the producer's patronage of the cooperative association.)

A producer would not be eligible for reimbursement if, at the time the claim was submitted, the producer owned at least 5% of the voting shares, other than publicly traded shares, membership interests, partnership interests, or other ownership interests of the parent corporation of the licensee whose failure was the basis of the claim.

In addition, a producer would not be eligible for reimbursement if title to the farm produce that was the subject of the claim had been transferred to the producer more than three years before the date the claim was submitted.

Currently, the board must deny the payment of a valid claim if it determines that the claimant has engaged in marketing practices that have contributed to the claimant's loss. In making its determination, the board may consider whether the marketing practices are generally accepted practices in this State. Under the bill, the board also would have to deny payment if it determined that the claimant had engaged in management practices that contributed to its loss, and the board could consider whether the management practices were generally accepted.

Fund Distribution; Audit

Section 17 of the Act requires the board to use money in the Fund only for a purpose described in the Act. If any portion of Section 17 is held to be invalid, the Act states legislative intent that the entire Act be held invalid and the money remaining in the Fund be distributed to producers in proportion to the amount of producer premiums each producer has paid to the authority. Under the bill, the money remaining in the Fund would have to be distributed to producers at the time and in the amounts established by the board.

Section 17 also requires all expenditures from the Fund to be audited by a certified public accountant (CPA) at least annually. Under the bill, the CPA would be selected by the board.

MCL 285.68 (S.B. 1396)
285.313 et al. (S.B. 1397)

ARGUMENTS

(Please note: The arguments contained in this analysis originate from sources outside the Senate Fiscal Agency. The Senate Fiscal Agency neither supports nor opposes legislation.)

Supporting Argument

Senate Bill 1396 would enable the MDA to respond more efficiently to changes in the economy by adjusting the license fees for grain dealers every year, rather than every three years. The bill would retain the current 5% limit on any adjustment, which protects both grain dealers and the Department from wide fluctuations in fees if the CPI changes by more than that percentage.

Supporting Argument

It no longer is necessary to require grain dealers who process and store produce to provide a surety bond or other security. With a current balance of \$6.2 million, the Farm Produce Insurance Fund is fiscally stable, and gives farm producers an economical way to cover their risk. Between the audits the MDA performs, and grain dealers' license criteria, which include a net asset requirement and a requirement that licensees maintain property insurance, this industry is adequately protected in Michigan.

Supporting Argument

By doubling the maximum amount that may be allocated each year from the Farm Produce Insurance Fund to the MDA, and clarifying that the money could be used for enforcement as well as administration, Senate Bill 1397 would address the Department's need for additional funding to inspect grain elevators. These inspections are important because the failure of an elevator can devastate the farmers who transferred produce to the facility. The failure of a large elevator also can have negative consequences for the entire community. Although every failure might not cause financial losses, elevator failures occur regularly, and the Department needs the resources to perform both audits and physical inspections in order to ensure that the facilities remain safe and solvent.

In addition, the bill would require the board of the Farm Produce Insurance Authority to enter into a memorandum of understanding (MOU) with the MDA Director for producer security services the Department performed for the Fund. Currently, according to the Department, MOUs are in place for administrative services based on a percentage of the investment balance.

Supporting Argument

Senate Bill 1397 would provide clarity regarding farm producers' eligibility for reimbursement from the Fund. The bill describes additional conditions under which a producer would not be eligible, including situations in which the producer had at least a 5% ownership interest in the licensed grain dealer's parent corporation, or the farmer had transferred title to the produce more than three years before submitting a claim. The bill also would authorize the board to deny a claim from a producer who

did not follow generally accepted management practices.

Supporting Argument

Senate Bill 1397 would allow the board of the Farm Produce Insurance Authority to select the CPA who will perform the annual audit of the Fund. Currently, according to the MDA, the Auditor General chooses the CPA.

Opposing Argument

By deleting the surety bond requirement for grain dealers who process and store farm produce (primarily grain elevators), Senate Bill 1396 would create additional exposure for the Farm Produce Insurance Fund that was not contemplated when total producer premiums were capped at \$5.0 million. Removing the bond requirement also would create additional risk for farm producers. Participation in the Fund is voluntary and some producers have opted out. If a nonparticipating farmer had transferred produce to an unbonded grain dealer, and the dealer went bankrupt, the farmer would have little chance of recovery. The Grain Dealers Act and the Farm Produce Insurance Act work in concert, and protections under both are necessary.

Legislative Analyst: Suzanne Lowe

FISCAL IMPACT

Senate Bill 1396

The bill would have an indeterminate impact on revenue to the Michigan Department of Agriculture from grain dealers' license fees. The bill would allow an adjustment of license fees annually rather than every three years. Whether the bill would result in a potential increase of revenue to the Department cannot be determined at this time, and would depend on the change in the Detroit consumer price index. In recent years, this change has ranged from a negative percentage to about 3%.

Senate Bill 1397

The bill would have an indeterminate impact on the MDA. The bill would increase the potential amount of revenue reimbursed to the Department from the Farm Produce Insurance Fund as it would raise the reimbursement cap from \$250,000 to \$500,000.

Fiscal Analyst: Bruce Baker

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This analysis was prepared by nonpartisan Senate staff for use by the Senate in its deliberations and does not constitute an official statement of legislative intent.