



Senate Fiscal Agency
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BILL ANALYSIS

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Senate Bills 1396 and 1397 (as enacted)
Sponsor: Senator Gerald Van Woerkom
Senate Committee: Agriculture and Bioeconomy
House Committee: Agriculture

PUBLIC ACTS 264 & 300 of 2010

Date Completed: 2-16-11

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. The Act requires participating farmers to 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 came up since the Fund began receiving money in 2005. Since the Fund covers the risk of a grain dealer's failure, some people believe that a surety bond is not needed from grain dealers who store produce if they are financially secure. In addition, it was suggested that the MDA should be able to adjust the license fee annually, rather than every three years as the law had allowed, to reflect changes in the consumer price index. The board that controls the Fund also recommended additional revisions, including clarification regarding producers' eligibility for reimbursement from the Fund.

CONTENT

Senate Bill 1396 amended 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 exempts a grain dealer who stores farm produce from the surety bond requirement if the dealer meets an asset-to-liability ratio and an equity ratio specified in the bill.

Senate Bill 1397 amended 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.**
- **Permit 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 is not eligible for reimbursement from the Fund.**
- **Require a valid claim to be denied if the claimant's management practices contributed to the loss, or if the claimant did not take reasonable actions to mitigate losses.**
- **Permit the board to select the certified public accountant to conduct the annual audit required under the Act.**
- **Permit the board to determine the distribution of money in the Fund if the Farm Produce Insurance Act is held invalid.**

Senate Bill 1396 took effect on December 14, 2010, and Senate Bill 1397 took effect on December 16, 2010.

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 is the administrator of the Fund for auditing purposes.

The Act previously authorized 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 could not exceed

5%, and had to be rounded to the nearest whole dollar.

The bill permits 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 must be rounded to the nearest \$5 increment.

Surety Bond Exception

Section 27(1) of the Act requires a grain dealer to give the MDA a bond that secures the dealer's warehouse receipts and open storage transactions, before a license is issued to the dealer. (This section applies to grain dealers that store and process grain.) The amount of the bond is based on the grain dealer's storage capacity.

Under the bill, notwithstanding Section 27(1), a grain dealer is not required to have a bond if the dealer files an audited financial statement that complies with Section 9 of the Act and that reports the following:

- A current asset to current liability ratio of 1.2 to 1.
- An equity ratio (equity/(total liability + equity) of 0.25 or greater.

(Section 9 requires a grain dealer to include a financial statement for the dealer's most recently completed year with an application for a license or renewal. The financial statement must be a reviewed or audited statement, prepared by a CPA, and must include an accountant's report, a balance sheet, an income statement, and a statement of the grain dealer's allowable net assets.)

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 the following:

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

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

The bill defines "producer security activities" as 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 permits the board of the Authority to enter into a memorandum of understanding with the MDA Director that provides for reimbursing the Director from the Fund for producer security activities.

The Farm Produce Insurance Act requires the board to allocate up to \$250,000 from the Fund annually to an administrative expenses account. The bill requires the account to be used to reimburse the Director for producer security expenses, in addition to paying 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 is ineligible for reimbursement if the claim relates to

delivery of farm produce to a licensee that is 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.

(The bill defines "cooperative association" as 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.)

Also, under the bill, a producer is not eligible for reimbursement if, at the time the claim is submitted, excluding patronage interests, the producer owns 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 is the basis of the claim. (The bill defines "patronage interests" as 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.)

In addition, the bill provides that a producer is not eligible for reimbursement if, at the time the claim is submitted, the producer is the owner of 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 is the basis of the claim.

A producer also is ineligible for reimbursement if title to the farm produce that is the subject of the claim was transferred to the producer more than two years before the date the claim is submitted.

Denial of Valid Claim

The Act requires the Authority board to 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 must deny payment if it determines that the claimant has engaged in management practices that contributed to its loss, and the board may consider whether the management practices are generally accepted.

In addition, the bill requires the board to deny payment of a valid claim if the board determines that the claimant did not take reasonable actions to mitigate farm produce losses.

(As amended by the bill, "valid claim" means a claim arising from a failure of a licensee that is found valid by the MDA and approved by the board, less all credits and offsets associated with farm produce delivered and sold in this State by a producer to a licensee or to a location in this State designated in advance of the delivery. The previous definition did not require the produce to be delivered, and did not refer to a location designated in advance.)

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. Previously, the Act required the money to be distributed in proportion to the amount of producer premiums each producer paid to the Authority. Under the bill, the money remaining in the Fund must 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 at least annually. Under the bill, the audit must be performed by a CPA 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 will 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 retains the 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 not necessary to require grain dealers who process and store produce to provide a surety bond or other security if they have adequate assets and equity. With a current balance of nearly \$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. Since Senate Bill 1396 requires a grain dealer to submit an audited financial statement reporting the required ratios, in order to be exempt from the bond requirement, the bill will ensure the necessary oversight that otherwise would come from the bonding process.

Supporting Argument

By clarifying that money in the Farm Produce Insurance Fund may be used for enforcement as well as administration, Senate Bill 1397 recognizes the Department's need for funding to inspect grain elevators. These inspections are important because the failure of an elevator can devastate the farmers who transferred produce to it. 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 permits 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 performs for the Fund. According to the Department,

MOUs already are in place for administrative services based on a percentage of the investment balance.

Supporting Argument

Senate Bill 1397 provides clarity regarding farm producers' eligibility for reimbursement from the Fund. The bill describes additional conditions under which a producer is not eligible, including situations in which the producer has at least a 5% ownership interest in the licensed grain dealer's parent corporation, or the farmer has transferred title to the produce more than two years before submitting a claim. The bill also authorizes the board to deny a claim from a producer who did not follow generally accepted management practices, or did not take reasonable steps to mitigate losses.

Supporting Argument

Senate Bill 1397 allows the board of the Farm Produce Insurance Authority to select the CPA who will perform the annual audit of the Fund. Previously, according to the MDA, the Auditor General chose the CPA.

Legislative Analyst: Suzanne Lowe

FISCAL IMPACT

Senate Bill 1396

The bill will have an indeterminate impact on revenue to the Michigan Department of Agriculture from grain dealers' license fees. The bill allows an adjustment of license fees annually rather than every three years. Whether the bill will result in a potential increase of revenue to the Department cannot be determined at this time, and depends 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 will have no fiscal impact on the MDA. The bill clarifies the existing provision allowing revenue to be reimbursed to the Department from the Farm Produce Insurance Fund for administrative costs, an amount that is approximately \$90,000 in FY 2010-11.

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.