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## **An Agricultural Law Research Article**

# **Grain Elevator Insolvencies and Help for the Producer: An Examination of the Bankruptcy Act of 1984**

by

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# Grain Elevator Insolvencies And Help For The Producer: An Examination Of The Bankruptcy Act of 1984\*

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## I. INTRODUCTION

On August 11, 1980, the owners of a chain of elevators doing business in southern Missouri and northern Arkansas filed a petition in bankruptcy with the Bankruptcy Court for the Eastern District of Arkansas.<sup>1</sup> Producers soon discovered that despite their apparent ownership of the grain, evidenced by warehouse receipts, they could not remove the stored grain from the elevators.<sup>2</sup> The Missouri Department of Agriculture, which under state law had taken control of the elevator three days prior to the bankruptcy petition, was prevented from operating or liquidating the Missouri locations.<sup>3</sup> It was determined that the grain claimed by the producers as their own was in fact property of the debtors to be administered under the jurisdiction of

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\*On July 10, 1984, the President signed the Bankruptcy Amendments and Federal Judgeship Act of 1984, which made significant changes in the Bankruptcy Code in several major areas. See H.R. 5174, 98th Cong., 2d Sess., 130 CONG. REC. H7489-7499 for complete text of the Act.

1. See *Missouri v. United States Bankruptcy Court*, 647 F.2d 768, 771 (8th Cir. 1981), cert. denied, 454 U.S. 1162 (1982). The James brothers operated the elevators under various partnership identities and one under corporate ownership.  
2. *Id.* at 772, n.7.  
3. *Id.* at 771.

the bankruptcy court.<sup>4</sup> This meant that any actions the producers would take regarding the ownership or distribution of the grain in question would be governed in large measure by the Bankruptcy Code and resolved in the bankruptcy court.<sup>5</sup> For the producer, this can mean expensive and lengthy litigation to recover grain that under the bailment created by the warehouse receipt would generally be considered his.<sup>6</sup>

Despite the publicity surrounding the unfair treatment of producers in the James brothers' bankruptcy, repeated attempts by the United States Senate to provide help had been blocked by the House of Representatives.<sup>7</sup> The House was forced to consider some change in the Bankruptcy Code after the United States Supreme Court declared the bankruptcy court system unconstitutional.<sup>8</sup>

This Article will examine the nature and magnitude of the problems caused by grain elevator insolvencies and the procedures available to the producer under the 1978 Bankruptcy Code. A number of common concerns have been expressed regarding the adequacy of the procedures. The provisions of the 1984 Act will be analyzed to determine to what extent the plight of the producer has been improved.

## II. BACKGROUND

### A. Nature and Magnitude of the Problem

To understand the nature of the problem one must understand the relationship between the producer and the elevator and the producer's need for the local elevator. The typical local elevator provides two major services to the producer. First, the elevator is a grain dealer.<sup>9</sup> As such, the elevator engages in various types of grain transactions including cash, credit, and commodity futures.<sup>10</sup> The elevator provides a local market whereby the producer can easily and readily sell his grain for either immediate payment or for a deferred price and

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4. *Id.* at 774.

5. *Id.*

6. See *infra* notes 24-29 and accompanying text.

7. As Senator Dole noted, "[f]ive times the legislation passed the Senate, while the House refused to take action." 130 CONG. REC. S8889 (daily ed.).

8. See *Northern Pipeline Constr. Co. v. Marathon Pipeline Co.*, 458 U.S. 50 (1982). The Court held that the creation of the bankruptcy courts by the Bankruptcy Act of 1978 was an unconstitutional exercise of congressional authority under art. I of the Constitution.

9. *Bankruptcy Reform Act of 1978 (Grain Elevator Insolvencies): Hearings on S. 839 Before the Subcomm. on Courts of the Senate Comm. on the Judiciary*, 97th Cong., 1st Sess. 32 (statement of Rep. Emerson) [hereinafter cited as *Elevator Insolvency Hearings*].

10. *Id.* at 105 (statement of Wallace Dick, Director of the Grain Warehouse Div., Iowa State Commerce Comm'n).

payment.<sup>11</sup>

A second, but equally important service is the storage of producer-owned grain, a commercial bailment agreement.<sup>12</sup> Producer use of elevators for temporary storage is necessitated by two factors. First, all grains are perishable, and therefore, must be stored in properly designed facilities to prevent loss from spoilage or other deterioration.<sup>13</sup> Second, the majority of producers do not have and cannot afford the investment required to have on premise storage for all of their production.<sup>14</sup> Without the option of storing their grain, the producer would be forced to sell a significant portion of his production as it is harvested.<sup>15</sup> Such a forced sale works a hardship on the producer by preventing him from possibly selling the grain at a later date for a higher price.<sup>16</sup> Being the only local market and knowing that the producer must sell at harvest time, the elevators could artificially depress prices.<sup>17</sup> Also, storage allows the producer who utilizes his grain in livestock production to store his production for the year and then take redelivery for use as feed when needed.<sup>18</sup>

Under the normal bailment agreement, the producer will deposit the grain in the elevator, receive a warehouse receipt evidencing ownership of the grain,<sup>19</sup> and pay a storage fee.<sup>20</sup> In return for the storage fee, the elevator agrees to return the grain, upon the owners demand, in the same condition as received.<sup>21</sup> Generally, the grain of any one producer is commingled with the stored grain of other producers and with grain owned by the elevator.<sup>22</sup> The commingling of the grain makes the holder of the warehouse receipt a tenant in common with respect to his proportionate share of grain stored in the elevator.<sup>23</sup>

The problems for the producer begin when the elevator, while still in possession of the grain under the bailment, files for protection under the Bankruptcy Code. When the producer presents the ware-

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11. *Id.*

12. *Id.* at 32.

13. Note, *A Survey of Current Issues and Legislation Concerning Grain Elevator Insolvencies*, 8 J. CORP. L. 111, 118 (1982).

14. *Id.*

15. *Id.*

16. *Id.*

17. *Id.*

18. *Id.*

19. *Id.* at 117.

20. *Elevator Insolvency Hearings*, *supra* note 9, at 32.

21. Note, *supra* note 13, at 118.

22. *Id.*

23. See *Preston v. United States*, 696 F.2d 528 (7th Cir. 1982), *modified*, 709 F.2d 488 (7th Cir. 1983), and *United States v. Luther*, 225 F.2d 499 (10th Cir. 1955), *cert. denied*, 350 U.S. 947 (1956). In the event of a shortage of grain at an elevator, the amount that each party is entitled to receive will be calculated using the *Preston* formula as set out in the modified opinion:

house receipt and demands return of his grain, he is denied his right of redelivery and repossession of the grain.<sup>24</sup> In *In re Missouri*,<sup>25</sup> it was firmly established that all stored grain is property of the bankrupt's estate,<sup>26</sup> and any disposition of such grain shall be determined by the bankruptcy court.<sup>27</sup> For the producer, this means any action to assert ownership, recover possession of the grain, or recover proceeds from the sale of the grain by the debtor will be heard in the bankruptcy court,<sup>28</sup> which must determine all ownership interests under applicable state law.<sup>29</sup>

It is worth noting the magnitude of the issue of grain elevator insolvencies. Between 1975 and early 1981 there were 177 grain elevator bankruptcies in the United States.<sup>30</sup> The bankruptcies represent approximately 2 percent of the 10,000 grain elevators nationwide.<sup>31</sup> Moreover, the number of bankruptcies per year has increased from fifteen in 1975 to thirty-seven in both 1979 and 1980.<sup>32</sup> The projection is that more elevators may be in financial trouble today than in the 1974 to 1981 period.<sup>33</sup>

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$$\text{Producers Share} = \frac{\text{Bushels represented by producers receipts}}{\text{Bushels represented by all receipts}} \times \text{Actual bushels in storage}$$

24. During hearings on S. 839 before the Comm. on the Judiciary, Rep. Bill Emerson quoted one farmer as saying:

Suppose you left your car in a public garage and received a parking receipt. Later you came back and hand the man a receipt and ask for your car. Could he tell me "You can't have your car back because the owner filed for bankruptcy and the bankruptcy judge appointed a trustee who will decide if you get your car back. If the trustee decides to sell your car you might have to sue to collect whatever you can after the trustees and the lawyers are paid their fees."

*Elevator Insolvency Hearings, supra* note 9, at 33.

25. 647 F.2d 768 (8th Cir. 1981), *cert. denied*, 454 U.S. 1162 (1982).

26. *Id.* at 774.

27. *Id.*

28. *Id.*

29. *Id.* The court noted that ownership rights of the various parties would be determined under Missouri law.

30. U.S. DEPT. OF AGRICULTURE, GRAIN ELEVATOR TASK FORCE, REPORT TO THE SECRETARY OF AGRICULTURE 47 (1981). The number of insolvencies reported by the Task Force may be unrealistically low because state officials may have counted only actual insolvencies and not cases in which operating licenses had been withdrawn prior to insolvency. *Id.* at 57.

31. UNITED STATES GENERAL ACCOUNTING OFFICE, MORE CAN BE DONE TO PROTECT DEPOSITORS AT FEDERALLY EXAMINED GRAIN WAREHOUSES i (1981) [hereinafter cited as GAO].

32. See GRAIN ELEVATOR TASK FORCE, *supra* note 30, at 48. The report was published in August, 1981.

33. A recent General Accounting Office survey of 400 randomly selected elevators indicated that 19 were in financial difficulty. If this estimated rate of 5 percent is

Losses suffered by producers as a result of elevator bankruptcies have been significant. During the six-year period from 1974 to 1979, 3,190 grain producers filed claims that totaled twenty-six million dollars.<sup>34</sup> Producers were able to recover about 28 percent of their claim, approximately seven million dollars.<sup>35</sup>

Nebraska ranked fifth in the number of actual bankruptcies reported<sup>36</sup> and seventh as to the number of elevators in financial difficulty.<sup>37</sup> While Nebraska's ranking is not as high as neighboring states, Nebraska producers should be concerned with the problems created by determination of their fate in the bankruptcy courts under the 1978 Bankruptcy Code.

### B. Source of the Bankruptcy Court's Jurisdiction

The control and operation of the Missouri locations brought into direct conflict the powers of the bankruptcy court and the regulatory powers of the Missouri Department of Agriculture. Each party asserted the right to control the disposition of the stored grain.<sup>38</sup> The Missouri Department of Agriculture, pursuant to state law, had taken control of all of the Missouri locations three days prior to the filing of the bankruptcy petition.<sup>39</sup> The Department also filed a receivership petition in the state circuit courts for all counties in which warehouses were located.<sup>40</sup> The state courts appointed a receiver and directed the receiver to, among other things, operate or liquidate any location to protect the best interest of the individuals having grain stored in the location.<sup>41</sup> The conflict escalated when the bankruptcy trustee filed a request to sell the grain in question free and clear of all liens.<sup>42</sup> The

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applied to approximately 10,000 elevators nationwide, an estimated 475 elevators could be in financial difficulty. The financial strength of elevators was measured by ratios and criteria developed by the agency. See GAO, *supra* note 31, at 13.

34. *Elevator Insolvency Hearings*, *supra* note 9, at 71.

35. *Id.* Non-farmers recovered considerably less, only 16 percent of their claim. *Id.* It should be noted, however, that the non-farm claims would include all unsecured creditors and could be misleading.

36. See GRAIN ELEVATOR TASK FORCE, *supra* note 30, at 47-48. According to records maintained by the Neb. Pub. Ser. Comm'n, there were six grain elevator bankruptcies in the five year period ending June 30, 1984. These failures resulted in a total dollar loss to producers of \$1,103,368.

37. GAO, *supra* note 31, at 13.

38. See *Missouri v. United States Bankruptcy Court*, 647 F.2d 768, 770 (8th Cir. 1981).

39. *Id.* at 771, n.6. MO. REV. STAT. § 411.519 authorized the Director of the Department to act as receiver to operate or liquidate a warehouse with insufficient inventory. See also MO. REV. STAT. § 411.519.6.

40. See *Missouri v. United States Bankruptcy Court*, 647 F.2d 768, 771 (8th Cir. 1981).

41. *Id.* The receiver was appointed one day after the bankruptcy petition was filed. The Director of the Mo. Dep't of Agriculture was appointed receiver. The receiver was also ordered to make an audit and a full investigation of the financial circumstances of the debtors. *Id.*

42. *Id.* at 772. The trustee relied on 11 U.S.C. § 363(f)(4) (1982), which permits the

trustee asserted a bona fide dispute as to the ownership of the stored grain.<sup>43</sup> The trustee also offered reasons in support of the request that were beneficial to all of the parties in interest.<sup>44</sup> Missouri obtained a state court restraining order that prohibited the trustee from interfering with the control, operation, and liquidation of the Missouri locations.<sup>45</sup> The trustee and bankruptcy court responded with a threat of contempt proceedings against the Director.<sup>46</sup> Missouri then unsuccessfully sought a writ of prohibition from the federal district court for the Eastern District of Arkansas.<sup>47</sup>

Missouri attacked the bankruptcy court's jurisdiction over the stored grain on the basis of Missouri law, which stated that grain was not the property of the warehouse owner but of the holder of the valid warehouse receipt.<sup>48</sup> The real question, however, was whether possession of the grain and the lien for storage fees were sufficient to meet the definition of property of the debtor under the Bankruptcy Code.<sup>49</sup> The legislative history and advisory notes to section 541 support the broad definition of property needed to bring stored grain within the control of the bankruptcy court.<sup>50</sup> The mere possession of stored grain is sufficient to bring it within the scope of section 541 and, therefore, under the jurisdiction of the bankruptcy court.<sup>51</sup> While the bankruptcy court has jurisdiction over stored grain, the court must administer the debtor's limited interest consistent with the ownership rights of all parties in interest.<sup>52</sup> The bankruptcy court must determine the ownership interests of all parties by application of appropri-

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sale of property owned by an entity other than the bankruptcy estate if the ownership is in bona fide dispute.

43. *Missouri v. United States Bankruptcy Court*, 647 F.2d 768, (8th Cir. 1981). The State of Missouri had earlier requested that the bankruptcy court determine the ownership of the grain, but voluntarily withdrew the request. At this point, the ownership of the grain was left in dispute and the door left open for the trustee's request for sale. *Id.* at 772.
44. In support of the request, the trustee noted the cost of continued storage, danger of deterioration, high market prices, and the financial benefits of investing the proceeds pending distribution to all of the parties in interest. *Id.* at 772.
45. *Id.* at 773.
46. *Id.*
47. *Id.*
48. *Id.* at 773-74.
49. 11 U.S.C. § 541 (1982).
50. H. R. REP. NO. 595, 95th Cong., 1st Sess. 367 (1977). The Report notes that: [U]nder paragraph (1) of subsection (a) [reference to 11 U.S.C. § 541], the estate is comprised of all legal or equitable interest of the debtor in property, wherever located, as of the commencement of the case . . . . The debtor's interest in the property also includes "title" to property, which is an interest just as are a possessory interest or leasehold interest for example.

*Id.*

51. See *Missouri v. United States Bankruptcy Court*, 647 F.2d 768, 774 (8th Cir. 1981).
52. *Id.* at 774.

ate state law.<sup>53</sup>

An alternate basis for state jurisdiction was an exception in section 362 for the exercise of police or regulatory powers.<sup>54</sup> The legislative history and advisory notes indicate that the purpose of the exception is to allow actions against the debtor to stop a violation of fraud, environmental protection, consumer protection, safety, or such similar police or regulatory laws.<sup>55</sup> The exception is intended to allow governmental units to take action in response to public health or safety, but not to protect a pecuniary interest in property of the debtor.<sup>56</sup> The action of the Missouri Department of Agriculture, although regulatory in nature, related primarily to the protection of the producers' pecuniary interest in the stored grain.<sup>57</sup> It appears that any state regulations that govern the operation or liquidation of an elevator would conflict with the administration of the property by the bankruptcy court and are not within the exception allowed under section 362(b)(4).<sup>58</sup>

The bankruptcy court would have jurisdiction under section 105<sup>59</sup> even if the actions of Missouri had been exempt under section 362. It may be that the bankruptcy court can enforce the stay on any action by the state.<sup>60</sup>

With the bankruptcy court possessing such broad power over the property of the debtor, the only option available to the producer or any state agency is action in the bankruptcy court. The remedies available are limited and may prove of little or no help to the producer. Also, it can take months or years to get a final determination of

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53. *Id.* See also *In re Clemens*, 472 F.2d 939, 942 (6th Cir. 1972); *In re Universal Medical Services Inc.*, 460 F.2d 524, 526 (3rd Cir. 1972); *In re Farmers Grain Exchange, Inc.*, 1 BANKR. CT. DEC. (CRR) 1621, 1622 (W.D. Wis. 1975).

54. "Except as provided in subsection (b) of this section, a petition filed under section 301 [voluntary petition], 302, or 303 [involuntary petition] of the title, . . . operates as a stay, applicable to all entities . . ." 11 U.S.C. § 362(a) (1982). The list of actions stayed is very broad. The exception is found in section 362(b)(4). It provides that such a filing shall not operate as a stay of commencement or continuation of an action or proceeding by a governmental unit to enforce its police or regulatory powers.

55. H. R. REP. NO. 595, *supra* note 50, at 343.

56. 124 CONG. REC. 32,395 (statement by Rep. Don Edwards, Chairman of subcomm. of the Judiciary Comm. considering the Bankruptcy Reform Act of 1978).

57. See *Missouri v. United States Bankruptcy Court*, 647 F.2d 768, 776 (8th Cir. 1981).

58. *Id.* However, it would appear that any regulation that relates directly to public health or safety could be enforced even if it affects the grain stored.

59. 11 U.S.C. § 105(a)(1982). The bankruptcy court may "issue any order, process, or judgment that is necessary or appropriate to carry out the provision of this title." *Id.*

60. See *Missouri v. United States Bankruptcy Court*, 647 F.2d 768, 776-77 (8th Cir. 1981). After holding that the police and regulatory exception of section 362(b)(4) did not apply, the court noted "even if applicable in this case [the exception] in no way deprives the bankruptcy court of jurisdiction over the bankrupt's estate . . ." *Id.* at 777.



an issue.<sup>61</sup>

### C. Potential Remedies for the Producer

The main objective of any action by the producer is the recovery of the stored grain or, in the alternative, the proceeds from any disposition of the stored grain. Several options are available to the producer. First, in a Chapter 7<sup>62</sup> liquidation proceeding, the producer may petition for an order requiring the trustee to release the grain held in storage.<sup>63</sup> Such action is only possible after the commencement of the liquidation proceeding but before any final distribution of the assets.<sup>64</sup> In addition, the grain in question must not have previously been disposed of under another section of the Act.<sup>65</sup> If the producer obtains the release of his grain, he may still be liable to the elevator for loading, handling, and storage charges related to the grain released.<sup>66</sup> If the amount recovered is less than the full amount due, the producer will have an unsecured claim for the balance.<sup>67</sup> In the case of less than full recovery, the producer might be allowed to set-off the charges against the amount of the shortfall.<sup>68</sup>

The abandonment provisions of section 554<sup>69</sup> are potentially available to the producer in all bankruptcy proceedings.<sup>70</sup> Under section 554(b), "On request of a party in interest and after notice and a hearing, the court may order the trustee to abandon any property of the estate that is burdensome . . . or that is of inconsequential value . . . ."<sup>71</sup> This section allows the producer to initiate the request for abandonment. When the debtor's interest is nominal, such as possession under a bailment with a lien for the storage charges, the producer can tender to the bankruptcy court the charges and strengthen his basis for abandonment.<sup>72</sup> Tendering the charges reduces the fear of loss of value to the estate and strengthens the argument that the grain is of

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61. See *infra* notes 80-84 and accompanying text for a detailed discussion of this area.

62. Chapter 7 proceedings are for a complete liquidation of all of the debtor's assets in a short period. Such proceedings are governed by 11 U.S.C. § 701-66 (1982).

63. See 11 U.S.C. § 725 (1982).

64. *Id.*

65. *Id.*

66. Looney & Byrd, *Protecting the Farmer in Grain Marketing Transactions*, 31 *DRAKE L. REV.* 519, 536 (1982).

67. *Id.*

68. 11 U.S.C. § 553 (1982).

69. *Id.* at § 554. Under section 554(a), the trustee may request the abandonment of any property. However, given the trustee's duty to the unsecured creditors, it is unlikely that the trustee would take such action regarding any stored grain. The producer would need to initiate any such action.

70. Chapters 1, 3 and 5, 11 U.S.C. § 101-559 (1982), are applicable to all bankruptcy proceedings.

71. 11 U.S.C. § 554(b) (1982).

72. See Looney & Byrd, *supra* note 66, at 536-37.

inconsequential value to the estate.<sup>73</sup> The producer will have the same rights to pursue a claim for any shortfall under section 554 as noted before under liquidation proceedings.<sup>74</sup>

Finally, the producer may seek relief from the automatic stay<sup>75</sup> and then proceed in state court for a determination of title to the grain.<sup>76</sup> If the producer is successful in establishing his title to the stored grain, the trustee is then forced to either turn over the grain or provide adequate protection.<sup>77</sup> In either case, the producer gains substantial leverage in the proceedings. Since there is no longer a bona fide dispute as to the ownership of the grain, the trustee's power to sell the grain under section 363(f) is eliminated.<sup>78</sup>

The remedies available to the producer are few. Even when successful, the remedies may be inadequate or too late to prevent substantial losses by the producer.

### III. INEQUITIES UNDER THE 1978 BANKRUPTCY CODE: THE NEED FOR A CHANGE

The events of the James Brothers case were symptomatic of similar problems experienced by farm producers and state Department of Agriculture officials in grain storage facility bankruptcies throughout the United States. Officials from the United States Department of Agriculture, state warehouse regulatory and licensing agencies, farm producer organizations, the National Grain and Feed Association, and representatives of various banking associations testified before a Senate Committee on the problems in warehouse bankruptcies in twenty-two midwestern and southeastern states.<sup>79</sup> Certain problems were repeatedly noted as hindering a speedy and proper distribution of grain assets.

First, the delays in the abandonment of the stored grain to the producers have commonly exceeded two years.<sup>80</sup> During such an extended period of time, the price of the grain may decrease dramatically, the condition of the grain may deteriorate, and the pro-

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73. *Id.*

74. See *supra* notes 67-68 and accompanying text for discussion of the term claim.

75. 11 U.S.C. § 362(d)(1982). The party requesting relief must establish the lack of adequate protection of their interest before the stay will be lifted. See *infra* note 77 for a discussion of adequate protection.

76. See *supra* note 53 and accompanying text.

77. See 11 U.S.C. § 361 (1982) for an explanation of adequate protection. While adequate protection is not defined, section 361 does provide three nonexclusive, non-exhaustive examples.

78. See *supra* note 42 and accompanying text.

79. See S. REP. NO. 65, 98th Cong., 1st Sess. 25-26 (1982).

80. *Id.* at 25. Any loss the producer might suffer because of price would be borne entirely by the producer. As to any loss because of quantity or condition, see *supra* note 21 and accompanying text.

ducer loses the use of the money. Second, conflicts in jurisdiction arise between the state agencies responsible for licensing and regulating elevators and the bankruptcy court regarding which party will control the grain during the bankruptcy proceedings.<sup>81</sup> Third, under the present law, the producer must share the grain assets held by the trustee on a pro rata basis with any creditor holding a security interest in assets of a similar type owned by the debtor. When there is a shortage of grain on hand, which is usually the case, the value of the producer's grain is diminished for the benefit of other creditors.<sup>82</sup> Fourth, some courts have been reluctant to accept warehouse receipts and scale tickets as evidence of ownership. Warehouse receipts and scale tickets are the principal ownership documents used in the industry.<sup>83</sup> Finally, certain bankruptcy courts have attached the stored grain for the payment of trustees' fees and expenses incurred for services unrelated to the stored grain. Again, the producer's asset is being unjustly diminished for the benefit of other creditors.<sup>84</sup>

With these common problems in mind, Congress added a section on grain elevator insolvencies to the 1984 Act. It was Congress' design to provide producers with procedures that would be both effective and efficient.

#### IV. THE 1984 ACT

As noted earlier, the Senate had made several attempts to improve the producers' situation. But until forced to do so by the *Marathon Pipe*<sup>85</sup> decision, the House refused to pass any relief legislation. The major focus of the 1984 Act was a reconstitution of the bankruptcy courts.<sup>86</sup> However, the Senate was able to include major changes in the areas of consumer credit, leasehold management, nondischargeability of debts incurred by drunk drivers, repurchase agreements, time share agreements, and grain elevator bankruptcies.<sup>87</sup>

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81. S. REP. NO. 65, *supra* note 79, at 25-26.

82. *Id.* See also *supra* note 23 and accompanying text. Nebraska Pub. Ser. Comm'n records indicated that in all six bankruptcies during the five year period ending June 30, 1984, the grain on hand was insufficient to meet the demands of all producers and secured creditors. Therefore, in all six cases the producer was forced to share his stored grain with secured creditors. Letter from Pamela S. Roesler, Staff Accountant, Neb. Pub. Serv. Comm'n, to Chris Quinn (July 10, 1984) (discussing grain elevator bankruptcies).

83. S. REP. NO. 65, *supra* note 79, at 25-26.

84. *Id.* Certain claims and expenses have priority over others in the determination of order and amount of payment. Generally, expenses of the trustee and lawyers will be a first priority. See 11 U.S.C. § 507(a)(1) (1982). See also *infra* note 131 and accompanying text.

85. Northern Pipeline Const. Co. v. Marathon Pipeline Co., 458 U.S. 50 (1982).

86. See generally Bankruptcy Amendments and Federal Judgeship Act of 1984, Pub. L. No. 98-353, § 101-211, 98 Stat. 333-51 (referred to in the text as the 1984 Act).

87. *Id.*

Several provisions were included in the 1984 Act that should assist the producers in dealing with an insolvent elevator.<sup>88</sup> The most significant and of the greatest potential benefit to a majority of producers is section 352.<sup>89</sup> This section provides for an expedited determination of ownership interests, abandonment, or any other disposition of the grain assets of the bankrupt elevator to the producer.<sup>90</sup> Two important aspects should be noted before any examination of the operation of the section. First, the section only applies in the case of a debtor that either owns or operates a grain storage facility.<sup>91</sup> However, the section only applies to the grain stored in the facility or the proceeds of such grain, and does not affect the application of any other sections of the Bankruptcy Code to all other property of the debtor.<sup>92</sup> Second, the section provides definitions for "grain,"<sup>93</sup> "grain storage facility,"<sup>94</sup> and "producer"<sup>95</sup> that are important.

The definition of producer is significantly different from that of "farmer"<sup>96</sup> used elsewhere in the Bankruptcy Code. An earlier Senate version conditioned the favorable treatment, not on being a producer, but upon possessing a "grain storage facility receipt."<sup>97</sup> This would have allowed any party to avail themselves of the expedited procedure.<sup>98</sup> The House and Senate records provide few if any guidelines on what activities are required to qualify as a party engaged in the growing of grain.<sup>99</sup> The individual involved in the day to day work of tilling the land, planting, and harvesting the grain should easily meet the requirement. However, it remains to be determined whether

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88. *Id.*

89. *Id.* at § 352 (to be codified at 11 U.S.C. § 557).

90. *Id.*

91. *Id.* at § 352(a) (to be codified at 11 U.S.C. § 557 (a)).

92. *Id.*

93. *Id.* (to be codified at 11 U.S.C. § 557(b)(1)). Grain includes wheat, corn, flaxseed, grain sorghum, barley, oats, rye, soybeans, rice, and dry edible beans.

94. *Id.* (to be codified at 11 U.S.C. § 557(b)(2)). Facility includes any site or structure regularly used to store grain for, or acquired for resale from, a producer.

95. *Id.* (to be codified at 11 U.S.C. § 557(b)(3)). Any entity that engages in growing of grain is entitled to utilize the section.

96. "'Farmer' means person that received more than 80 percent of such person's gross income during the taxable year of such person . . ." 11 U.S.C. § 101(17) (1982). It should be noted that the definition here is restrictive to prevent some individuals from utilizing the favorable treatment received by farmers when they file bankruptcy. See, e.g., 11 U.S.C. § 303 (1982), which prohibits the filing of an involuntary petition against a farmer.

97. See S. REP. NO. 65, *supra* note 79, at 65-66. Any document of the type routinely issued by the facility evidencing ownership of the grain would have been considered a grain storage facility receipt.

98. Under such a definition, a lender who has obtained a warehouse receipt as security for a loan, or a processor or grain dealer who had purchased grain from the elevator but left it in storage could use the procedures. Under the producer definition of the 1984 Act, they would not be considered a producer.

99. See *supra* note 91.

an individual who is an owner of land and receives part of the production from the land as rent will be considered a producer under section 557. It was noted that the section was intended to include bona fide family farm corporations but not large corporate farming operations.<sup>100</sup> Exactly how far the definition of producer can be extended will be decided by the bankruptcy court as various parties attempt to avail themselves of the expedited procedures. Certainly, the more directly an individual can tie his ownership of the grain to the production of the grain, the greater the probability of his being considered a producer.

Perhaps the most important provision of the section is the requirement for an expedited treatment of actions relating to the stored grain.<sup>101</sup> The section establishes a 120 day period for the completion of any applicable procedure allowed under section 557.<sup>102</sup> Upon consideration of one or more of the factors set out in section 557(c)(2), the court may determine a time table of less than 120 days for the disposition of the issue.<sup>103</sup> Several of the factors may be of considerable assistance to the producer in his attempt to shorten the 120 day period. When the condition of the stored grain is deteriorating, and will continue if the grain remains in storage, a prompt disposition of the grain would benefit all parties. If the market price of the grain is expected to decline and remain below current levels, an immediate sale of the grain and an investment of the proceeds pending distribution would be in everyone's best interest. Any exposure of the grain to loss or dete-

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100. See 130 CONG. REC. H1817 (daily ed. Mar. 21, 1984). (Statement of Rep. Glickman, Chairman of the Ad Hoc Subcommittee on Grain Elevator Bankruptcies of the Committee on Agriculture). Here again, no guidelines were given on what constitutes a bona fide family corporation or a large corporate operation.

101. Bankruptcy Amendments and Federal Judgeship Act of 1984, Pub. L. No. 98-353, § 352(a), 98 Stat. 333, 359 (to be codified at 11 U.S.C. § 557(c)(1)).

102. *Id.* See *infra* notes 104-14 and accompanying text for discussion of procedures allowed.

103. Bankruptcy Amendments and Federal Judgeship Act of 1984, Pub. L. No. 98-353, § 352(a), 98 Stat. 333, 359 (to be codified at 11 U.S.C. § 557(c)(2)). The Code provision states:

The court shall determine the extent to which such time periods shall be shortened, based upon:

- (A) Any need of an entity claiming an interest in such grain or the proceeds of grain for a prompt determination of such interest;
- (B) Any need of such entity for a prompt disposition of such grain;
- (C) The market for such grain;
- (D) The conditions under which such grain is stored;
- (E) The costs of continued storage or disposition of such grain;
- (F) The orderly administration of the estate;
- (G) The appropriate opportunity for an entity to assert an interest in such grain; and
- (H) Such other considerations as are relevant to the need to expedite such procedures.

*Id.*

rioration of quality caused by the nature or condition of the storage facility should prompt the court to resolve the problem quickly and economically. While an immediate sale may not be possible, the grain could be moved to a different facility until final disposition.

A potential conflict exists, however, over the continued storage of the grain or an immediate sale. The producer will want to dispose of the grain and terminate his obligation for storage. The trustee may want to continue collecting fees for as long as possible. The fees will generate more dollars for the benefit of the estate. Neither party should be required to bear additional storage costs for any length of time without a resulting benefit. The court should weigh the cost benefit ratio to each party on the storage issue. Any shortened time period set by the court must be of sufficient length to afford all parties who have an interest in the grain to assert their rights. However, if the producer complies with the notice requirements of the Bankruptcy rules<sup>104</sup> when seeking a shortened period, this requirement does not pose any significant problems. Finally, the provision allowing for consideration of all relevant factors will allow the producer to plead any special facts or circumstances that might exist. The more factors that the producer can establish, the greater the likelihood that the court will shorten the 120 day period. Even one factor may be adequate to persuade the court.

The actions subject to expedited treatment are limited.<sup>105</sup> The allowable procedures are a claim of ownership,<sup>106</sup> a proof of claim,<sup>107</sup> a request for abandonment,<sup>108</sup> a request for relief from the section 362(a) automatic stay,<sup>109</sup> and a request for a determination of secured status.<sup>110</sup> Also included are all requests for a determination of whether the grain or proceeds of the grain is property of the estate,<sup>111</sup> must be turned over to the estate,<sup>112</sup> or sold.<sup>113</sup> In addition, the expe-

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104. BANKR. RULE 2002. The general notice requirements of the rule range from twenty to thirty days. For example, under 2002(c), a party can sell an asset of the estate and give only twenty days notice of the sale.

105. See Bankruptcy Amendments and Federal Judgeship Act of 1984, Pub. L. No. 98-353, § 352(a), 98 Stat. 333, 359 (to be codified at 11 U.S.C. § 557(d)).

106. This would include all claims of ownership made pursuant to applicable state law. See *supra* notes 52-53 and accompanying text.

107. This would include all proof of claims filed pursuant to BANKR. RULES 3001, 3002, and 3003.

108. This would include all claims made pursuant to 11 U.S.C. §§ 554 & 725 (1982). See *supra* notes 63-65 and 69-73 and accompanying text.

109. This would include any request made pursuant to 11 U.S.C. § 362(b), (c) or (d) (1982).

110. This would include all requests made pursuant to 11 U.S.C. §§ 545-46 (1982).

111. Property of the estate is governed by 11 U.S.C. § 541 (1982), with all questions of ownership rights to be determined by applicable state law. See *supra* notes 48-53 and accompanying text.

112. 11 U.S.C. §§ 542-43 (1982) govern turnover of property to the estate.

dated procedures apply to any disposition of the grain or the proceeds of the grain by way of sale, abandonment, distribution, or any other equitable method.<sup>114</sup> No new substantive procedures were added by the 1984 Act, and all of the above procedures were available under the 1978 Bankruptcy Code. The difference is the time and priority in which a producer can force a resolution of the issue by the bankruptcy court.

Under the 1978 Code, the producer had no priority over other creditors with an interest in the grain assets. The producer was forced to share his stored grain with other creditors having a security interest in the grain assets. The producer was treated as a secured creditor despite his actual ownership of the stored grain.<sup>115</sup> The legislative intent of the expedited procedures of section 557 was to correct this "forced sharing."<sup>116</sup> Section 557 requires the court to distribute either the stored grain or the proceeds thereof to the producer before any distribution to secured creditors.<sup>117</sup> This means that all of the grain in a facility, whether stored by the producer or owned by the debtor, will first be used to satisfy the claims of producers for grain stored under a bailment. Such a priority in the distribution of the grain assets should greatly reduce the amount of loss suffered by the producer. The loss will be shifted, and properly so, to the secured creditor. The combination of the priority treatment and the shortened time frame for the distribution should prove extremely beneficial to the producer.

Despite being denied the right to exercise their regulatory powers once an elevator files for bankruptcy,<sup>118</sup> the state regulatory units did gain some power by virtue of the 1984 Act. A state regulatory unit may initiate any action allowed under the new section.<sup>119</sup> The provision gives the agency some control over the grain or the proceeds. One of the major benefits to the producer could be a single action by the regulatory agency. The proceedings could apply to the interest of all producers in the stored grain. Such an action would reduce the cost of litigation for the producer and increase the chances for a favorable outcome. In addition, the trustee must consult with the regulatory agency before taking any action related to the disposition, custody, or

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113. The trustee under 11 U.S.C. § 363 (1982), has power, in certain circumstances, to sell assets of the estate. *See supra* notes 42-43.

114. Bankruptcy Amendments and Federal Judgeship Act of 1984, Pub. L. No. 98-353, § 352(a), 98 Stat. 333, 359 (to be codified at 11 U.S.C. § 557(d)(2)).

115. *See supra* note 82 and accompanying text.

116. *See* S. REP. NO. 65, *supra* note 79, at 26. The Senate expressed a similar intention during consideration of an earlier proposed revision of the bankruptcy code. *See* S. REP. NO. 168, 97th Cong., 1st Sess. 9, 16 (1981).

117. *See supra* notes 90 and 95 and accompanying text.

118. *See supra* notes 54-60 and accompanying text.

119. Bankruptcy Amendments and Federal Judgeship Act of 1984, Pub. L. No. 98-353, § 352(a), 98 Stat. 333, 359 (to be codified at 11 U.S.C. § 557(e)).

control of the grain or the proceeds of the grain.<sup>120</sup> The state agency will thus be aware of any action that might be adverse to the producer's interest and appropriately intervene on behalf of the producers.

One potential problem exists for the producer under the 1984 Act. Realizing that there could be circumstances under which the 120 day period would work an undue hardship on a party, Congress provided an exception. The court may extend the 120 day period, provided the interests of a claimant are not materially injured.<sup>121</sup> Since the major purpose of the bankruptcy provisions is the protection of the debtor, the courts may construe this discretionary power to the detriment of the producer. What constitutes a material injury will normally be a question of fact to be determined on a case-by-case basis. Also, it is uncertain if all producers must be treated equally. What may be material to one producer may not be to another producer, such as the amount of grain in question.

Most of the evidence presented by the parties in any action under section 557 may be unfamiliar to the court. The court, to aid itself in the evaluation of the evidence, may appoint a trustee or examiner and retain professional help.<sup>122</sup> The use of such individuals should insure that proper consideration is given to the evidence presented with any request.

The trustee cannot delay carrying out any order under section 557 unless such action is stayed pending an appeal.<sup>123</sup> In the event an order is reversed or modified on appeal, all actions taken before the reversal or modification remain valid.<sup>124</sup> While this may at times work to the detriment of the producer, it should prevent the trustee from bringing spurious appeals simply to gain additional time. In many instances, the action will be completed before the appeal can be resolved.

The 1984 Act directly addresses the problem of the use of the stored grain to pay unrelated administrative expenses.<sup>125</sup> The trustee shall only recover from the grain or the proceeds of the grain the reasonable and necessary expenses attributed to either preserving or disposing of the grain or proceeds.<sup>126</sup> The dollar amounts in the trustee compensation scale will include the value of any grain distributed by the trustee in kind.<sup>127</sup> This procedure should solve the problem of the

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120. *Id.*

121. *Id.* (to be codified at 11 U.S.C. § 557(f)).

122. *Id.* (to be codified at 11 U.S.C. § 557(d)(3)).

123. *Id.* (to be codified at 11 U.S.C. § 557(g)).

124. *Id.*

125. *See supra* note 84 and accompanying text.

126. Bankruptcy Amendments and Federal Judgeship Act of 1984, Pub. L. No. 98-353, § 352(a), 98 Stat. 333, 359 (to be codified at 11 U.S.C. § 357(b)).

127. *Id.*



producer while providing adequate compensation to the trustee. The trustee can pursue all reasonable alternatives with the assurance of being paid for his services.

There may be some instances where the producer would prefer re-delivery of the grain.<sup>128</sup> In a majority of the cases redelivery will not be an option. In all cases where the quantity of a specific grain held by the debtor exceeds ten thousand bushels the grain will be sold.<sup>129</sup> The proceeds of the sale will then be subject to expedited treatment under section 557.<sup>130</sup> If prices have increased during the period, the amount of the proceeds received by a producer may not be sufficient to purchase the same amount of grain stored. Under such circumstances, the producer will suffer a direct loss for which he will have no claim against the debtor.

As previously noted, the filing of the bankruptcy petition prohibited the producer from reclaiming his grain. Under the 1984 Act, the producer now has a very limited right of reclamation.<sup>131</sup> To qualify, the grain must have been delivered while the elevator was insolvent and a written request for reclamation made within ten days of delivery.<sup>132</sup> A proper request can only be denied if the court secures the producer's claim by a lien.<sup>133</sup> In either event, the producer has greatly improved his position and likelihood of recovery. The ten-day requirement will limit the use of this section to a very few "lucky" producers.

Section 557 includes one other benefit for the producer. If a producer does not recover the full amount of his claim by the priority distribution of the grain assets, any shortage would be an unsecured claim.<sup>134</sup> However, to the extent of \$2,000, the producer is granted a fifth priority in payment.<sup>135</sup> Such priority would allow payment to the producer in advance on any payment to almost all other creditors.<sup>136</sup> Any shortage in excess of the \$2,000 priority will remain an unsecured claim. The producer will receive payment, if any, as set out in the

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128. *See supra* note 18 and accompanying text.

129. Bankruptcy Amendments and Federal Judgeship Act of 1984, Pub. L. No. 98-353, § 352(a), 98 Stat. 333, 359 (to be codified at 11 U.S.C. § 557(i)).

130. *Id.*

131. *Id.* at § 351 (to be codified at 11 U.S.C. § 546(d)).

132. *Id.*

133. *Id.* *See* 11 U.S.C. § 506 (1982) for benefit and value to the producer of a secured lien.

134. *See generally* 11 U.S.C. §§ 501-06 (1982).

135. Bankruptcy Amendments and Federal Judgeship Act of 1984, Pub. L. No. 98-353, § 350, 98 Stat. 333, 358 (to be codified at 11 U.S.C. § 507(a)(5)). Those claims allowed in advance of the producer's claim are (1) administrative expenses; (2) unsecured claims allowed under 502(f); (3) unsecured claims for wages, salaries or commissions; and (4) unsecured claims for contributions to employee benefit plans. 11 U.S.C. § 507 (1982). *See also supra* note 84.

136. *Id.*

debtors plan and approved by the bankruptcy court.<sup>137</sup>

The 1984 Act made one significant change in the Bankruptcy Rules. Under Rule 3001, warehouse receipts, scale tickets, or other documents routinely issued by grain storage facilities as evidence of title are to be recognized by the court as prima facie evidence of grain ownership.<sup>138</sup> The rule applies so long as it is not inconsistent with either the United States Warehouse Act or state law.<sup>139</sup> Under the new rule, the producer should have little difficulty in establishing his ownership interest.

All of the changes noted under section 557 and Rule 3001 became effective on October 7, 1984.<sup>140</sup> The changes apply only to cases commenced after the effective date.<sup>141</sup> All cases commenced before the effective day will continue to be governed by the 1978 Bankruptcy Code. For some extended period of time all producers will not be treated equally. The "lucky" ones will be able to use the new provision to obtain a faster more equitable return of their grain, while the "unlucky" continue to struggle with the problems and frustrations of the old law.

## V. CONCLUSION

The 1984 Act was designed to provide efficient and effective help for the producer in elevator bankruptcies. The new provisions do give the producer a greater chance of timely and equitable recovery of his stored grain. If the bankruptcy courts apply the provisions as suggested here, producers will have the help they deserve. However, should the new provisions fail to improve the producers' situation, any additional help may be difficult to obtain without another major crisis in the bankruptcy area. The fate of the producer still rests with the bankruptcy courts.

*Roger Dunekacke, '86*

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137. See generally 11 U.S.C. §§ 721-28, 1121-71, 1321-30 (1982).

138. Bankruptcy Amendments and Federal Judgeship Act of 1984, Pub. L. No. 98-353, § 354, 98 Stat. 333, 361 (to be codified at Bankruptcy Rule 3001(g)).

139. *Id.* In Nebraska, a scale ticket shall be issued to the owners upon delivery of the grain. The ticket shall be prima facie evidence of the holder's ownership. NEB. REV. STAT. §§ 88-505, 505.01 (1981).

140. Bankruptcy Amendments and Federal Judgeship Act of 1984, Pub. L. No. 98-353, § 553(a), 98 Stat. 333, 392.

141. *Id.*