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Dealing with Grain Dealers: The Use of State Legislation to Avert Grain Elevator Failures

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Notes

Dealing with Grain Dealers: The Use of State Legislation to Avert Grain Elevator Failures

On January 30, 1980, the owner of the Prairie Grain Company of Stockport, Iowa borrowed a pickup truck from one of his employees when state inspectors arrived unexpectedly to examine his elevator's books. He then drove the truck down a highway, pulled off onto a side road, and shot himself to death.[1] He left behind a grain elevator that ultimately declared bankruptcy.[2] Officials estimated that Prairie Grain's total losses would exceed $10,000,000,[3] which included over $6,000,000 in farmers' claims for grain either stored by or sold to Prairie Grain.[4] One farmer suffered a loss of nearly $100,000.[5] Another farmer suffered a $27,000 loss, which put him out of business.[6] A third farmer, who had just paid off the mortgage on his farm, was back in debt and unable to turn the farm over to his son, as previously planned.[7] Most of the farmers filing claims in the bankruptcy proceeding would receive at most ten cents on the dollar for their grain.[8]

Although grain producers, as a group, were the biggest losers, the effects of the Prairie Grain Company failure were felt by many others. Various companies and banks that did business with Prairie Grain sustained combined losses totaling $4,000,000.[9] The federal government was also among the top money losers in the Prairie Grain scandal.[10] Finally,

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1. Braun, *Last Trip to Stockport*, FARM J., June-July 1980, at 13.

2. Des Moines Register, Apr. 1, 1980, at 1A, col. 5. The elevator was unable to account to farmers for 1,203,939 bushels of corn, 531,325 bushels of soybeans, 10,079 bushels of wheat, and 9303 bushels of oats. *Id.* at 5A, col. 3.

3. *Id.*

4. *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. 106 (1981) (statement of E. Wallace Dick, Director of the Grain Warehouse Division, Iowa State Commerce Commission) [hereinafter cited as *Hearings*].

5. Letter from Lowell E. Gose, President of the Iowa Farmers Union, to Floyd Millen, Iowa State Representative (Mar. 11, 1980) (concerning problem of grain elevator failures) (on file with the *Iowa Law Review*).

6. Des Moines Register, Aug. 17, 1980, at 2B, col. 5.

7. Braun, *Last Trip to Stockport*, FARM J., June-July 1980, at 14-15.

8. *Hearings, supra* note 4, at 149 (statement of Reuben L. Johnson, Director of Legislative Services, National Farmers Union).

9. Braun, *Last Trip to Stockport*, FARM J., June-July 1980, at 14.

10. Des Moines Register, Mar. 21, 1980, at 3A, col. 1. Federal loans totaling $793,000 had been secured with grain that grain producers were storing at the elevator. The grain

merchants of Stockport and the surrounding communities were affected by a decline in business following the bankruptcy.[11]

Grain producers are forced to take many risks. While growing their crops, producers are threatened by insects, floods, drought, wind, and hail. After the crop is harvested, grain producers face a further risk of being forced to sell the crop at a price level that leaves them without a profit. Even if grain producers overcome the odds and harvest a plentiful and profitable crop, they often may face one more risk—the risk of the potential failure of the elevator to which they have taken grain for storage or sale. However, proper legislation can minimize the risk of grain elevator failure, thereby reducing the number and amount of resulting losses.[12]

The purpose of this Note is to examine the provisions of the current Iowa grain dealer statute and potential amendments to the existing statutory provisions in light of the causes and effects of grain dealer failures. Initially, an overview of the magnitude of the problems caused by grain elevator failures will demonstrate the importance of effective legislation.[13] A consideration of the relationship between federal and state grain elevator legislation will indicate the necessity of effective state legislation.[14] Then, in order to evaluate the utility of various legislative provisions and proposals, this Note will focus on the causes of grain elevator failures.[15] Next, the provisions of the current Iowa grain dealer statute will be analyzed to discover the advantages, disadvantages, and effectiveness of each provision.[16] Finally, potential amendments to the Iowa statute will be considered, and a method for determining an optimal combination of statutory requirements will be outlined.[17]

I. THE NEED FOR EFFECTIVE LEGISLATION

A. The Magnitude of the Problem

In order to appreciate the need for legislation, it is helpful to examine the extent of the problem of grain elevator bankruptcies and their effects on the lives of grain producers and others. Between 1975 and early 1981,

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producers considered giving up their rights to the grain rather than continuing to repay the loans. *Id.*

11. *Hearings, supra* note 4, at 107 (statement of E. Wallace Dick, Director of the Grain Warehouse Division, Iowa State Commerce Commission). One of the gas stations in Stockport closed, the restaurant closed, and automobile and farm implement dealers were affected adversely because only bare necessities were purchased by farmers after the bankruptcy. *Id.*

12. *See* Statement of Dean Kleckner, President of the Iowa Farm Bureau Federation, to the Iowa House Agriculture Committee, at 1 (Mar. 17, 1981) (regarding grain marketing) (on file with the *Iowa Law Review*).

13. *See* text accompanying notes 18-42 *infra*.

14. *See* text accompanying notes 43-71 *infra*.

15. *See* text accompanying notes 72-83 *infra*.

16. *See* text accompanying notes 84-142 *infra*.

17. *See* text accompanying notes 143-212 *infra*.

there were 177 grain elevator bankruptcies in the United States,[18] representing about two percent of approximately 10,000 grain elevators nationwide.[19] Moreover, the number of bankruptcies has increased during the past seven years. Only fifteen elevator bankruptcies were reported in 1975, while thirty-seven bankruptcies were reported in both 1979 and 1980.[20]

The losses suffered by grain producers as a result of elevator bankruptcies have been significant. During the six-year period from 1974 to 1979, 3190 grain producers filed grain elevator bankruptcy claims, which totaled $26,000,000.[21] By the end of 1979, however, grain producers had recovered only about $7,000,000, or twenty-eight percent of their claims.[22] Over the same six-year period, the average loss per grain producer per elevator bankruptcy was $4292, and average losses ranged from zero in five instances to $23,535 in one elevator bankruptcy.[23]

Unfortunately, more grain elevators may be in financial trouble today than were in the past. According to a recent General Accounting Office survey of 400 elevators, nineteen—close to five percent of the total—were in financial difficulty.[24] If the percentage results of that General Accounting Office survey are applied to the universe of 10,000 grain elevators nationwide, an estimated 475 elevators conceivably may be in financial difficulty today.[25] Although that estimate certainly does not indicate that 475 elevator bankruptcies will occur in the near future, it does suggest cause for concern.[26]

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18. GRAIN ELEVATOR TASK FORCE, U.S. DEP'T OF AGRICULTURE, REPORT TO THE SECRETARY OF AGRICULTURE 47 (1981). The number of grain elevator 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.

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

20. *See* GRAIN ELEVATOR TASK FORCE, *supra* note 18, at 48. The Task Force's report was published on August 18, 1981. Therefore, the number of bankruptcies reported for 1981 is not a total year-end figure that can be compared to figures for other years.

21. *Hearings, supra* note 4, at 71 (report of the Illinois Legislative Council). The report reproduced in the Senate hearings is entitled "Grain Elevator Bankruptcies in the U.S.: 1974 through 1979" and was prepared for the Illinois Legislative Council and the U.S. Department of Agriculture, in cooperation with the Illinois Department of Agriculture.

22. *Id.* Nonfarmers recovered considerably less—only $527,070, or 16% of their claims. *Id.* The farmer and nonfarmer losses might have been reduced, however, by recoveries made after 1979. *Id.*

23. *Id.* at 74. The average was based on 30 bankruptcies in which the data regarding farmers was complete. *Id.*

24. GAO, *supra* note 19, at 13. The General Accounting Office randomly selected the sample of 400 elevators from among the 6321 Commodity Credit Corporation contract grain elevators. *Id.* The General Accounting Office determined that the 19 elevators were in financial difficulty by applying certain financial ratios and self-developed criteria to financial data collected from the sample elevators. *Id.* at 12.

25. *See id.* at 13.

26. *See id.*

Iowa has the regrettable distinction of ranking first in the nation in the number of grain elevator bankruptcies reported between 1975 and early 1981.[27] Iowa, with thirty-five grain elevator bankruptcies—approximately twenty percent of the total number of bankruptcies reported—far outdistanced the runner-up, Indiana, which reported twenty-two bankruptcies.[28] Iowa also led the nation in the number of grain elevators that, though not bankrupt, were found by the General Accounting Office to be in financial difficulty;[29] of the nineteen elevators that were found to be financially troubled, six were located in Iowa.[30]

B. Social and Economic Effects of Grain Elevator Bankruptcies

The full magnitude of the problems caused by grain elevator failures is not revealed by an examination of statistics alone. The social and economic impact of grain elevator bankruptcies on grain producers and local farm communities is great. For instance, grain producers who are unable to recover all of their losses in bankruptcy proceedings may be forced to sell all or part of their land and machinery, refinance their operations, or forego expansion of their farms.[31] Even if grain producers with claims against a bankrupt elevator ultimately recover all of their claims, they often are affected adversely by the delay in elevator bankruptcy proceedings.[32] While courts attempt to deal with the legal difficulties inherent in bankruptcy, the money owed to grain producers is not available for the grain producers' use.[33] Because the unavailable funds are frequently the sole source of financing for the next year's planting, the viability of entire farm operations may be jeopardized by the delay.[34]

Another negative effect on grain producers that results from grain elevator bankruptcies concerns the commodity markets in the areas where

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27. *See* GRAIN ELEVATOR TASK FORCE, *supra* note 18, at 47-48.

28. *See id.*

29. GAO, *supra* note 19, at 14.

30. *Id.*

31. *Hearings, supra* note 4, at 66 (statement of Thomas D. Hopkins, Coordinator of the Grain Regulatory Services Program, Division of Grain Inspection and Warehousing, Missouri Department of Agriculture).

32. *Id.* at 65. Currently, there are two bills before Congress that, if passed, would require expedited abandonment of grain that is required to be abandoned under provisions of the bankruptcy code and is held by a debtor in bankruptcy who operates a grain storage facility. These bills also create a priority position in favor of grain producers with respect to the distribution of assets to general unsecured creditors in bankruptcy. *See* H.R. 6034, 97th Cong., 2d Sess. (1982); S. 1365, 97th Cong., 1st Sess. (1981). See Looney & Byrd, *Protecting the Farmer in Grain Marketing Transactions*, 31 DRAKE L. REV. 519 (1981-82), and Note, *A Survey of Current Issues and Legislation Concerning Grain Elevator Insolvencies*, 8 J. CORP. L. 111 (1982), for discussions of federal bankruptcy issues relating to grain elevators.

33. *See* Meyer, *Keeping Harvests Safe from Failing Elevators*, FARMLINE, Aug. 1981, at 4.

34. *Hearings, supra* note 4, at 65 (statement of Thomas D. Hopkins, Coordinator of the Grain Regulatory Services Program, Division of Grain Inspection and Warehousing, Missouri Department of Agriculture).

the bankruptcies occur. After an elevator bankruptcy, grain producers tend to store their grain in larger elevators, which are thought to be more sound financially than smaller elevators.[35] Because the larger elevators may be farther from the grain producers' fields, delay and transportation costs add to the overall cost of grain merchandising.[36] Increased delivery costs result in less net proceeds for producers. More important, when farmers begin to patronize only the larger elevators, smaller elevators may be forced out of business.[37] As the number of elevators decreases, competition for grain may decrease, and the decrease in competition may result in even lower prices for producers.[38]

Others, in addition to grain producers, feel the adverse effects of a grain elevator bankruptcy. Creditors, such as banks that loaned money to the elevator and businesses that dealt with the elevator, also sustain losses.[39] Moreover, the entire local farm community suffers when an elevator bankruptcy occurs, because the negative impact is spread throughout the community.[40] The grain elevator is generally one of the larger employers in a rural community; therefore, many residents of the community lose their jobs when an elevator fails.[41] Local businesses also suffer because the money generated by the elevator is removed from the community.[42] The detrimental social and economic effects of grain elevator bankruptcies, which are felt by grain producers, local businesses, and entire communities, clearly demonstrate a problem in need of attention.

II. STATUS OF FEDERAL AND STATE GRAIN ELEVATOR LAWS

A brief examination of the relationship between federal and state grain elevator legislation serves to demonstrate the importance of effective state

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35. *See id.* at 59 (statement of Laurence H. Earle, Director of the Indiana Commodity Dealers Licensing Agency).

36. *See id.*

37. *Id.* at 114.

38. *Id.*

39. *See id.* at 112. On Aug. 6, 1982, the Mount Pleasant Bank and Trust Company was declared insolvent and ordered closed by Iowa state banking officials. Des Moines Register, Aug. 7, 1982, at 1A, cols. 1-2. The bank's failure was caused by a series of loan losses, including losses associated with the bankruptcy of the Prairie Grain Company, which owed the bank $2,200,000 at the time of its collapse. *Id.* It seems, however, that the bank had a hand in its own destruction. In a state trial court suit brought by 120 Stockport-area farmers against the bank, the jury found that the bank had conspired to defraud the farmers and awarded them $2,100,000 in damages. Des Moines Register, Oct. 1, 1982, at 5S, cols. 4-6. The farmers had alleged that the bank continued to lend money to Prairie Grain and its owner even though the bank officials knew that Prairie Grain was insolvent. *Id.*

40. *Hearings*, *supra* note 4, at 66 (statement of Thomas D. Hopkins, Coordinator of the Grain Regulatory Services Program, Division of Grain Inspection and Warehousing, Missouri Department of Agriculture).

41. *Id.*

42. *Id.* For a discussion of what happened in one community, see note 11 *supra* and accompanying text.

legislation. The United States Warehouse Act[43] was enacted in 1916 to provide a uniform federal regulatory system governing warehouses that store agricultural products.[44] The major purpose of the Act is to facilitate proper financing of the stored products.[45] The Act does not require all warehouses to be licensed in accordance with its provisions, but merely offers those that apply and qualify for licenses an alternative to state regulation.[46] Therefore, a grain warehouseman can elect to be licensed by federal or state authorities. However, when a warehouseman elects to be regulated by the Warehouse Act, the matters regulated by the Act, which include most important matters, cannot be regulated by the state.[47]

Grain warehouses licensed under the Warehouse Act must meet requirements for sound warehouse operations. Some of the requirements that must be met to qualify for a federal license include furnishment of an acceptable bond,[48] maintenance of a minimum net worth,[49] and payment of inspection and licensing fees.[50] Once licensed under the Act, warehousemen are subject to periodic, unannounced examinations.[51] In addition, they must issue detailed warehouse receipts for products stored[52] and may be punished by fine or imprisonment for violation of the Act.[53]

Federally licensed grain warehouses, as well as state licensed and unlicensed warehouses, must comply with Commodity Credit Corporation (CCC) standards if they have contracts with the CCC.[54] In carrying out its various price-support programs, the CCC, a federally established corporation, contracts with warehouses for the storage of commodities that it owns or that have been pledged to it as collateral for government loans.[55] The standards that CCC-contract warehouses must meet are similar to those of the Warehouse Act.[56] The major difference between the two sets

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43. 7 U.S.C. §§ 241-273 (1976).

44. 10 N. HARL, AGRICULTURAL LAW § 74.01, at 74-2 to -3 (1981).

45. *See id.*

46. *Id.* at 74-3.

47. Rice v. Santa Fe Elevator Corp., 331 U.S. 218, 234 (1947); 7 U.S.C. § 269 (1976); D. UCHTMANN, J. LOONEY, N. KRAUSZ & H. HANNAH, AGRICULTURAL LAW: PRINCIPLES AND CASES § 12.5, at 414 (1981).

48. 7 U.S.C. § 247 (1976); 7 C.F.R. §§ 102.13-.17 (1982). The Secretary of Agriculture has power to "make such rules and regulations as he may deem necessary for the efficient execution of the [warehouse provisions]." 7 U.S.C. § 268 (1976).

49. 7 C.F.R. § 102.6 (1982).

50. 7 U.S.C. § 251 (1976); 7 C.F.R. §§ 102.57-.60 (1982).

51. 7 U.S.C. §§ 243, 264-267 (1976); 7 C.F.R. § 102.39 (1982). The Agricultural Marketing Service, a division of the United States Department of Agriculture, administers the licensing and examination program under the Warehouse Act. GAO, *supra* note 19, at 1.

52. 7 U.S.C. §§ 259-260 (1976); 7 C.F.R. §§ 102.18-.32 (1982).

53. 7 U.S.C. § 270 (1976).

54. 7 C.F.R. § 1421.5551 (1982). The CCC has power under 15 U.S.C. § 714b(d) (1976) to adopt regulations governing the manner in which its business may be conducted.

55. GAO, *supra* note 19, at 2. CCC storage contract functions are carried out by the Agricultural Stabilization and Conservation Service, a division of the USDA. *Id.*

56. *Id.*

of standards is that the CCC does not require warehouse operators to be bonded.[57]

Approximately twenty-nine states have laws that regulate grain elevators, but these laws differ significantly from state to state.[58] The purpose of all state grain elevator legislation, however, is to provide protection and security for grain producers to ensure that they receive payment for the grain that they market.[59] State legislation can be divided into two categories: preventive and remedial.[60] Preventive provisions include licensing, minimum net worth requirements, and annual inspections.[61] Remedial provisions provide the means of compensating grain producers who suffer losses when grain elevators fail despite the existence of preventive provisions.[62] Examples of remedial provisions are those requiring bonding and indemnity funds.[63] If state grain elevator legislation is to be effective, it must include both adequate preventive and remedial provisions.[64]

This Note will be limited to the examination of *state* legislation pertaining to the regulation of grain elevators.[65] A focus on state law is important for two reasons. First, grain warehousemen who do not elect to be licensed under the Warehouse Act and who also do not contract with the

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57. *Id.* For specific standards, see 7 C.F.R. §§ 1421.5551-.5557 (1982).

58. GAO, *supra* note 19, at 3.

59. Testimony of Neil Hamilton, Assistant Attorney General in the Farm Division of the Office of the Iowa Attorney General, to the Iowa Grain Elevator and Grain Grading Joint Subcommittee, at 2 (Aug. 19, 1980) (on file with the *Iowa Law Review*).

60. *See id.* Hamilton refers to preventive provisions as indirect loss protection measures and to remedial provisions as direct loss protection measures.

61. *Id.*

62. *See id.* at 2-3.

63. *Id.* at 3.

64. *See id.* at 3-4.

65. Proposals have been proffered for a mandatory federal grain warehousing/dealing statute, which would preempt all present federal and state laws on grain warehousing and dealing. The statute would contain both preventive and remedial provisions. *See* GRAIN ELEVATOR TASK FORCE, *supra* note 18, at 10-16. One advantage of a preemptive federal statute is that it would offer a nationwide, uniform administration program. *Id.* at 16. Also, it would eliminate dual federal-state regulation and duplication of effort, thereby reducing the costs of licensing, bonding, and inspection programs. *Id.* However, there are also disadvantages associated with an exclusively federal program. One problem is that the federal statute would preempt state jurisdiction and nullify many state prerogatives, thereby prompting controversy, which could delay or impair an effective federal program. *Id.*

It also has been suggested that the federal government should expend its time and effort in states with inadequate grain dealer laws. *Hearings, supra* note 4, at 67 (statement of Thomas D. Hopkins, Coordinator of the Grain Regulatory Services Program, Division of Grain Inspection and Warehousing, Missouri Department of Agriculture). States with acceptable regulations would be exempt from the provisions of the federal statute. GRAIN ELEVATOR TASK FORCE, *supra* note 18, at 14-15. Although the federal government has been considering a mandatory federal grain warehousing/dealing statute for some time, Iowa and other states cannot afford to wait and see what happens on the federal scene and must act now to solve the grain elevator bankruptcy problem.

CCC are subject solely to state regulation.[66] Therefore, because only about 6400 grain warehouses, out of the estimated 10,000 grain warehouses nationwide, are subject to the federal requirements of the Warehouse Act or the CCC,[67] approximately 3600 warehouses are regulated solely by state law.

More significantly, consideration of state law is important because, although the warehouse activities of grain elevators may be subject to federal or state regulation, the activities of dealers are subject only to state regulation.[68] The difference between grain elevators that are warehouses and those that are dealers is that warehouses store grain, whereas dealers purchase and sell grain or, in other words, merchandise grain.[69] Consideration of state regulation of the dealer activities of grain elevators is important because dealer practices by grain elevators may be one of the main causes of grain elevator bankruptcies.[70] Moreover, state laws governing grain dealers affect most grain elevators because elevators typically are involved in both warehousing and dealing.[71]

III. CAUSES OF GRAIN ELEVATOR BANKRUPTCIES

To be effective, preventive legislation should address one or more of the causes of grain elevator bankruptcies. However, there are two causes of elevator bankruptcies that can only be indirectly controlled by legisla-

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66. *See* GAO, *supra* note 19, at 3.

67. *Id.*

68. *See* D. UCHTMANN, J. LOONEY, N. KRAUSZ & H. HANNAH, AGRICULTURAL LAW: PRINCIPLES AND CASES § 12.5, at 416 (1981).

69. *Id.* The Iowa Legislature has defined "grain dealer" as

> a person who buys during any calendar month five hundred bushels of grain or more from the producers of the grain for purposes of resale, milling, or processing. However, "grain dealer" shall not be construed to mean a producer of grain buying for his or her own use as seed or feed; a person solely engaged in buying grain future contracts on the board of trade; a person who purchases grain only for sale in a registered feed; a person engaged in the business of selling agricultural seeds regulated by chapter 199; a person buying grain only as a farm manager; or an executor, administrator, trustee, guardian, or conservator of an estate; or a bargaining agent as defined in section 542A.1.

Act of June 13, 1981, ch. 180, § 1, 1981 Iowa Acts 564, 564-65 (to be codified as amended at IOWA CODE § 542.1(3)).

"Warehouse" is defined as "any building, structure, or other protected enclosure in this state used or usable for the storage of agricultural products." IOWA CODE § 543.1(2) (1981). There are approximately 825 grain warehouses and 1900 grain dealers licensed in Iowa. IOWA STATE COMMERCE COMM'N, 1979 ANNUAL REPORT 6.

70. *See Hearings*, *supra* note 4, at 41 (statement of John R. Block, U.S. Secretary of Agriculture).

71. D. UCHTMANN, J. LOONEY, N. KRAUSZ & H. HANNAH, AGRICULTURAL LAW: PRINCIPLES AND CASES § 12.5, at 416 (1981).

Because most problems derive from grain dealing, this Note will concentrate on state legislation that regulates grain dealers. However, most of what is written will be relevant to grain warehouse legislation as well. The only section of this Note that will not be rele-

tion. One of those causes is the state of the economy.[72] The fact that commercial and industrial failures rose fifty-five percent in 1980 for all businesses indicates that business failures due to the state of the economy are not unique to the grain business.[73] Therefore, there is not much that legislation can do to eliminate the state-of-the-economy cause of grain elevator bankruptcies. However, legislation can provide for early detection of elevators suffering financial difficulty as a result of the state of the economy and, thereby, prevent or minimize losses.[74] The second cause of elevator bankruptcies that cannot be directly controlled by legislation is fraud by elevator operators.[75] However, although legislation cannot prevent a determined fraud, various regulations make fraud more difficult.[76] Legislators also can enact stiff criminal penalties to deter elevator operators from intentionally violating grain elevator laws.

There are, however, causes of grain elevator bankruptcies that state legislation can affect directly. Two causes, reported by the states as the main causes of elevator bankruptcies, are speculation in the futures market and poor management.[77] A third cause of grain elevator bankruptcies that

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vant to grain warehouse legislation is the section accompanying notes 146-74 *infra*, pertaining to delayed pricing.

Although this Note will use Iowa law as a basis for analysis, the analysis also may be used to test the adequacy of other states' grain dealer statutes.

72. GRAIN ELEVATOR TASK FORCE, *supra* note 18, at 47.

73. *Id.*

74. *See generally Hearings, supra* note 4, at 106 (statement of E. Wallace Dick, Director of the Grain Warehouse Division, Iowa State Commerce Commission).

75. *See* Leidahl, *USDA Softening Approach to Bankruptcy Safeguards for UGSA Grain Warehouses*, FEEDSTUFFS, Dec. 1981, at 3, 42; *see also* GRAIN ELEVATOR TASK FORCE, *supra* note 18, at 49-51 (many states reported possible criminal activity as a cause of past grain elevator bankruptcies).

Fraud was one cause of the Prairie Grain Company bankruptcy. *See* Des Moines Register, Apr. 1, 1980, at 1A, cols. 5-6. The day before a state inspection was to begin, the owner of the Prairie Grain Company would write checks for grain that had been delivered to the elevator to give the appearance that the company was paying for grain on a daily basis. Then, when the inspectors left, the owner would void the checks and destroy the settlement sheets that served as receipts for purchased grain. *Id.*

76. *See* Leidahl, *USDA Softening Approach to Bankruptcy Safeguards for UGSA Grain Warehouses*, FEEDSTUFFS, Dec. 1981, at 3, 42 (quoting James Springfield, Director of the Warehouse Division of the Agricultural Marketing Service). Two examples of state legislative provisions that make fraud by elevator operators more difficult are the requirement of frequent mandatory inspections of grain elevators' premises, books, and records by state regulatory personnel and the prelicense requirement of the submission of an annual financial statement, accompanied by an unqualified opinion based on an audit performed by a certified public accountant.

The Iowa grain dealer statute provides that "[a] person who knowingly submits false information to or knowingly withholds information from the commission or any of its employees when required to be submitted or maintained under this chapter, commits a fraudulent practice." Act of June 13, 1981, ch. 180, § 11, 1981 Iowa Acts 564, 570 (to be codified as amended at IOWA CODE § 542.11(1)).

77. *Hearings, supra* note 4, at 70, 77 (report of the Illinois Legislative Council). Some people think that speculation in the futures market is the "basic problem in most elevator

legislation can deal with directly, and that is considered by some to be responsible for many grain elevator bankruptcies,[78] is delayed pricing.[79] Delayed pricing occurs when an elevator receives grain under a contract that provides for the pricing of the grain at a later date.[80] If state legislation designed to prevent grain elevator bankruptcies from occurring is to be productive, it must deal with one or more of these causes of grain elevator bankruptcies.

Legislative preventive measures represent the most important form of protection available to grain producers. If preventive measures are carefully structured to deal with the causes of grain elevator bankruptcies, they will prevent the majority of bankruptcies from occurring.[81] However, while legislative remedial measures hopefully would be employed infrequently, they are very important when preventive measures fail,[82] as they inevitably will on occasion. Therefore, an efficient grain regulatory program should include a mixture of both preventive and remedial legislative provisions.[83] The preventive provisions should be designed to prevent, either directly or indirectly, one or more of the causes of grain elevator bankruptcies that can be controlled by legislation, including fraud, poor management, delayed pricing, and speculation. It is questionable, however, whether Iowa has a balanced and well-reasoned legislative program that contains appropriate preventive and remedial provisions and that deals with all of the major causes of grain elevator bankruptcies.

IV. THE IOWA GRAIN DEALER STATUTE

A. New Prelicense Requirements to Alleviate Poor Management Practices

The Iowa grain dealer[84] statute, chapter 542 of the Iowa Code,[85] was amended in 1981[86] in response to public outcry over the Prairie Grain

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failures." Statement by William Carter, farmer from Stockport, Iowa, to the Iowa Grain Elevator and Grain Grading Joint Subcommittee (on file with the *Iowa Law Review*).

78. Des Moines Register, Feb. 24, 1980, at 2F, col. 5 (quoting Maurice Van Nostrand, former chairman of the Iowa Commerce Commission and a former grain elevator operator).

79. Delayed-pricing contracts are sometimes referred to as deferred-pricing contracts, price-later contracts, or no-price-established contracts. *Watch Out for Price Later Pitfalls*, WALLACES FARMER, Oct. 24, 1981, at 9. The Iowa statute refers to the contract as a "credit-sale contract." Act of June 13, 1981, ch. 180, § 3, 1981 Iowa Acts 564, 565 (to be codified at IOWA CODE § 542.1).

80. D. Good, Delayed Pricing by Country Elevators 1 (Sept. 1977) (Illinois Agricultural Economics Staff Paper, University of Illinois, Urbana-Champaign, No. 77 E-22).

81. *See* Testimony of Neil Hamilton, *supra* note 59, at 2-3. Of course, the operability of legislative preventive measures depends on an adequate enforcement mechanism. *See* text accompanying notes 131-38 *infra*.

82. *See* Testimony of Neil Hamilton, *supra* note 59, at 3.

83. *Id.*

84. For the Iowa statutory definition of "grain dealer," see Act of June 13, 1981, ch. 180, § 1, 1981 Iowa Acts 564, 564-65 (to be codified as amended at IOWA CODE § 542.1(3)), *reproduced at* note 69 *supra*.

85. IOWA CODE ch. 542 (1981).

86. Act of June 13, 1981, ch. 180, 1981 Iowa Acts 564.

Company disaster.[87] Among other changes and additions, three prelicense conditions were added to the grain dealer statute. The three new conditions that must be met before a grain dealer will be licensed are: (1) maintenance of a minimum net worth, (2) submission of an annual financial statement, and (3) maintenance of a minimum current assets to current liabilities ratio.[88] All three of these conditions are preventive in nature and are directed at one of the major causes of grain elevator bankruptcies: poor management.[89] In order to prevent major losses and minimize future losses, early detection of poor management is a primary objective of grain dealer legislation.[90] Moreover, the requirement that financial statements be accompanied by either a certified public audit or review will make grain dealer fraud more difficult.

Although all elevators that deal in grain must meet the three prelicense conditions, the Iowa Legislature has established a two-class license system for grain dealers, with different standards applicable to each class.[91] A class one license is required if the grain dealer purchases any grain by credit-sale contract,[92] or if the value of the grain purchased by the dealer during the previous year exceeded $250,000.[93] If purchases were less than or equal to $250,000, a class two license is sufficient.[94] The major difference between the standards applicable to the two classes is that class two net worth and financial statement standards are less strict than those of class one.[95]

To some extent, the imposition of lesser standards on small grain dealers is probably a necessary reflection of their lower volume of business.[96] Regulations that are too stringent might force some small grain dealers out of business because the costs of complying with the stringent require-

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87. *See* Des Moines Register, Sept. 27, 1980, at 5A, col. 1.

88. Act of June 13, 1981, ch. 180, § 4, 1981 Iowa Acts 564, 566-67 (to be codified at IOWA CODE § 542.3(4), (5)).

89. *Hearings, supra* note 4, at 70, 77 (report of the Illinois Legislative Council).

90. *See* Letter from Twila Morris, Iowa Commerce Commission, to the Iowa Grain Elevator and Grain Grading Joint Subcommittee (on file with the *Iowa Law Review*).

91. Act of June 13, 1981, ch. 180, § 4, 1981 Iowa Acts 564, 565 (to be codified at IOWA CODE § 542.3(2)).

92. "Credit-sale contract" means "a contract for the sale of grain pursuant to which the sale price is to be paid more than thirty days after the delivery of the grain to the buyer." *Id.* § 3, 1981 Iowa Acts at 565 (to be codified at IOWA CODE § 542.1). "Credit-sale contract" includes contracts referred to as deferred-payment contracts, deferred-pricing contracts, and price-later contracts. *Id.*, 1981 Iowa Acts at 565.

93. *Id.* § 4, 1981 Iowa Acts at 565 (to be codified at IOWA CODE § 542.3(2)(a)). Any grain dealer whose grain purchases did not exceed $250,000 may elect to be licensed as a class one grain dealer. *Id.*, 1981 Iowa Acts at 565.

94. *Id.*, 1981 Iowa Acts at 565 (to be codified at IOWA CODE § 542.3(2)(b)).

95. *Compare id.*, 1981 Iowa Acts at 566 (class one license requirements) (to be codified at IOWA CODE § 542.3(4)), *with id.*, 1981 Iowa Acts at 566-67 (class two license requirements) (to be codified at IOWA CODE § 542.3(5)).

96. Iowa Grain Warehouse and Grain Grading Joint Subcommittee of the Committees on Commerce, Minutes 7 (Sept. 18, 1980) (statement of Thomas D. Hopkins, Coordinator of the Grain Regulatory Services, Missouri Department of Agriculture).

ments would be too great.[97] However, many commentators associated with the grain industry think that the grain dealer statute's prelicense requirements should be equally stringent for large and small volume dealers.[98] Although the "equal treatment" view might appear to be unreasonably harsh as applied to small volume dealers, some commentators think it is justified because of the greater tendency for small grain dealers to go bankrupt.[99] The Iowa Legislature, however, apparently thought that small volume dealers posed a less significant threat to the well-being of grain producers and seemingly attempted to balance the hardship on small grain dealers with the interests of grain producers by establishing the two-class system.

The prelicense requirement of the submission of an annual financial statement, accompanied by an unqualified opinion based on an audit performed by a certified public accountant,[100] has been the focus of much of the controversy over the recent amendment to chapter 542.[101] The main concern centers around the costliness of audits.[102] However, the usefulness

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97. *See* WALLACES FARMER, Nov. 8, 1980, at 16.

98. *See, e.g.*, Statement of Donald E. Johnson, Chairman of the Legislative Committee of the Iowa Grain and Feed Association, to the Iowa Grain Elevator and Grain Grading Joint Subcommittee, at 3-4 (Mar. 17, 1981) (on file with the *Iowa Law Review*); Summary of Testimony Offered at Public Hearing on the Iowa Grain Merchandising & Warehouse Bill, at 1 (testimony of Orland Fara and Lyle Kucera) (on file with the *Iowa Law Review*).

99. *Hearings, supra* note 4, at 70, 74-75 (report of the Illinois Legislative Council). This report showed that 47% of the bankrupt elevators included in the survey had storage capacities of less than 100,000 bushels and that 84% had capacities under 300,000 bushels. Only 5% of the bankrupt elevators had capacities larger than 1,000,000 bushels. *Id.*

100. Act of June 13, 1981, ch. 180, § 4, 1981 Iowa Acts 564, 566 (to be codified at IOWA CODE § 542.3(4)(b)). Only class one grain dealers are required to submit a financial statement accompanied by an *unqualified opinion* based on a certified public accountant *audit*. Class two grain dealers need only submit a financial statement accompanied by a *report* based on a certified public accountant *review*. *Id.*, 1981 Iowa Acts at 566-67 (to be codified at IOWA CODE § 542.3(5)(b)).

The scope of the examination required by the grain dealer statute to obtain an unqualified opinion based on an audit is much more extensive than that required for a report based on a review. An unqualified opinion based on an audit states that "the financial statements present fairly financial position, results of operations and changes in financial position in conformity with generally accepted accounting principles (which include adequate disclosure) consistently applied." AUDITING STANDARDS EXECUTIVE COMM., AM. INST. OF CERTIFIED PUB. ACCOUNTANTS, STATEMENT ON AUDITING STANDARDS No. 28, at 10 (Oct. 1974).

101. *E.g.*, Letter from David P. Miller, President and Owner of Batavia Grain, Inc., to the Iowa Grain Elevator and Grain Grading Joint Subcommittee, at 6 (Aug. 19, 1980) (on file with the *Iowa Law Review*); Summary of Testimony Offered at Public Hearing on the Iowa Grain Merchandising & Warehouse Bill, at 1 (testimony of William Harbor) (on file with the *Iowa Law Review*).

102. *See* Summary of Testimony Offered at Public Hearing on the Iowa Grain Merchandising & Warehouse Bill, at 1-3 (testimony of William Harbor, Gary Fairbanks, Jerald Kunce, and John Ridgely) (on file with the *Iowa Law Review*); Keith, *Revolutionary Changes Being Considered in Government Warehouse Programs*, GOVERNMENT & GRAIN, Oct. 15, 1981, at 2. Estimates on the range of the cost of audits vary from $1000 to $7000, Iowa Grain

of the financial information obtained from audits is thought to far outweigh the burden imposed on grain dealers.[103]

Financial information is useful beyond its initial employment as an indication of the solvency of a grain dealer. The Iowa Commerce Commission, the agency that regulates Iowa grain dealers,[104] can use the financial information for at least two additional purposes after licenses have been issued. First, the information can be used to aid Commission inspectors in their annual inspections of the premises, books, and records of grain dealers.[105] Second, the information can be used by the Commission to determine the order in which to inspect elevators and whether to inspect them more often than the statute requires.[106] The information obtained from audited financial statements also can be helpful to grain dealers,[107] some of whom realize that audited financial statements can be the best management tool a grain dealer can purchase.[108]

Warehouse and Grain Grading Joint Subcommittee of the Committees on Commerce, Minutes 5 (Sept. 18, 1980) (statement of James Onken, Chief of Bureau of Warehouses, Illinois Department of Agriculture), to $3000 to $5000, GRAIN ELEVATOR TASK FORCE, *supra* note 18, at 24, to $2000 to $3000, Letter from David P. Miller, President and Owner of Batavia Grain, Inc., to the Iowa Grain Elevator and Grain Grading Joint Subcommittee, at 2 (Aug. 19, 1980) (on file with the *Iowa Law Review*).

103. Illinois is considered to have good, tough grain industry legislation, *see* Des Moines Register, Feb. 24, 1980, at 1F, col. 1, and Illinois officials consider their audit provision to be one of the most crucial provisions of their recently strengthened law, Testimony of Neil Hamilton, *supra* note 59, at 5. The Iowa State Commerce Commission views audited financial statements as the most important enforcement tools that can be implemented by state legislatures. Letter from Twila Morris, Iowa State Commerce Commission, to the Iowa Grain Elevator and Grain Grading Joint Subcommittee (on file with the *Iowa Law Review*).

104. IOWA CODE §§ 542.1(1), 542.2 (1981).

105. *See* Meyer, *Keeping Harvests Safe from Failing Elevators*, FARMLINE, Aug. 1981, at 6 (quoting Merrill Marxman, member of the Grain Elevator Task Force and area director with the USDA's Agricultural Stabilization and Conservation Service). Section 542.9 is the Iowa provision governing inspection of premises, books, and records. *See* Act of June 13, 1981, ch. 180, § 10, 1981 Iowa Acts 564, 569-70 (to be codified as amended at IOWA CODE § 542.9).

106. *See generally* GRAIN ELEVATOR TASK FORCE, *supra* note 18, at 23. Section 542.9 requires the Iowa Commerce Commission to inspect the premises, books, and records of all grain dealers at least once a year. Act of June 13, 1981, ch. 180, § 10, 1981 Iowa Acts 564, 569-70 (to be codified as amended at IOWA CODE § 542.9). However, the Commission has the authority to inspect any grain dealer more frequently than once a year. *See id.*

107. *See* GRAIN ELEVATOR TASK FORCE, *supra* note 18, at 23, 32. Certified public accountant audits reveal items easily ignored, overlooked, or hidden by company accountants. *Id.* at 23. The audits can help grain dealers determine which parts of their operations are efficient and which need improvement. *See id.* at 32.

108. Statement of Donald E. Johnson, Chairman of the Legislative Committee of the Iowa Grain and Feed Association, to the Iowa Grain Elevator and Grain Grading Joint Subcommittee, at 3 (Mar. 17, 1981) (on file with the *Iowa Law Review*); *see also* Summary of Testimony Offered at Public Hearing on the Iowa Grain Merchandising & Warehouse Bill, at 2 (testimony of Jerald Kunce) (on file with the *Iowa Law Review*).

The effectiveness of audited financial statements in preventing grain elevator bankruptcies is suggested by the experience of Iowa cooperative grain elevators. Each cooperative elevator is required to undergo a certified audit and to present a statement of its financial condition to its membership annually.[109] Cooperative elevator directors firmly believe that annual audited financial statements are an essential tool that can be used by elevators to prevent financial problems.[110] Their optimism concerning the effectiveness of annual audited financial statements may have basis in fact because, of the thirty-five Iowa grain dealer and warehouse licenses that were revoked for financial reasons over a recent five and one-half year period, only one of the licenses belonged to a cooperative elevator.[111] Yet, approximately one-fourth of Iowa's licensed elevators are cooperatives.[112] The positive experience of cooperative elevators with annual audited financial statements supports the conclusion that Iowa's new prelicense requirement of the submission of an annual financial statement, accompanied by an unqualified opinion based on an audit performed by a certified public accountant, might be a step in the right direction.

The Iowa Legislature also might consider the use of a predictive formula for grain dealers. The information obtained from audited financial statements could be plugged into the formula to aid the state licensing agency in its evaluation of grain dealers.[113] Dealers could also evaluate their own firms using a predictive model.[114] Mathematical formulas have been developed for predicting bankruptcies in other industries and could be developed specifically for the grain industry.[115] In fact, research already has been done on the development of an early warning model for grain

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109. Des Moines Register, Feb. 24, 1980, at 2F, col. 1.

110. *See* Braun, *Last Trip to Stockport*, FARM J., June-July 1980, at 15 (quoting Ron McCleary, a cooperative director).

111. *See* Des Moines Register, Feb. 24, 1980, at 2F, col. 1.

112. In 1980 there were approximately 185 cooperative elevators and 615 privately owned elevators licensed under the Iowa grain elevator statute. Report of the Iowa Commerce Commission to the Iowa Grain Elevator and Grain Grading Joint Subcommittee (Nov. 12, 1980) (letter from Wallace Dick, Director of the Grain Warehouse Division) (on file with the *Iowa Law Review*).

There is a difference of opinion concerning the financial healthiness of cooperative grain elevators, and at least one authority thinks that cooperative elevators encounter as many financial problems as privately owned elevators. *See id.* Moreover, there are other differences between cooperative and privately owned elevators, besides the cooperative elevator requirement of an annual audited financial statement, that may have an impact on the financial health of cooperative grain elevators. *See* Des Moines Register, Feb. 24, 1980, at 2F, col. 1. A major difference between cooperative elevators and privately owned elevators is that the organizational structure of cooperative elevators is such that the owners of the elevators are the grain producers who are storing or selling their grain at the elevators. These owners, or members, elect the directors of the cooperative elevators, who set much of the policy followed by the elevator managers. *See id.*

113. Siebert, *Credit Rating Formula Aids Elevator Management*, FEEDSTUFFS, Mar. 15, 1982, at 31.

114. *Id.*

115. GAO, *supra* note 19, at 9. Accurate formulas have been developed for manufac-

elevators.[116] The development and implementation of a predictive formula deserves legislative consideration.

B. More Stringent Bonding, Inspection, and Penalty Provisions

The 1981 amendment to the Iowa grain dealer statute also strengthened previously existing bonding, inspection, and penalty provisions. One provision that was strengthened, the bonding provision, is a prelicense remedial provision. Applicants for class one grain dealer licenses must now file a bond of $50,000, and a bond of $25,000 is required for class two licenses.[117] Before the 1981 amendment, all grain dealers were required to file a $25,000 bond.[118] While the bonding provision is a remedial provision, the amount of money provided by the bond is not enough to compensate grain producers fully for losses incurred because of the failure of a licensed grain dealer's business, unless the losses are small.[119] For example, bond money constituted less than five percent of the estimated liabilities in the Prairie Grain Company failure.[120] Increasing bonding requirements to provide grain producers with full protection would be excessive, however, because it would be too costly for both grain dealers and grain producers.[121] Grain producers arguably would bear most of the costs because the bonding costs likely would be passed on by the dealers to the producers in the form of lower prices for their grain.[122]

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turing firms and railroads. Also, the Federal Deposit Insurance Corporation uses a formula to monitor banks. *Id.*

116. *See generally* J. Siebert, Financial Performance of Country Elevators (Sept. 1980) (Cooperative Extension Service, Purdue University, No. EC-516). A detailed analysis of the economic and statistical procedures used in Dr. Siebert's research may be found in J. Siebert, Early Warning Models for Grain Elevator Bankruptcy (Dec. 1981) (University of California, Davis).

117. Act of June 13, 1981, ch. 180, § 5, 1981 Iowa Acts 564, 567 (to be codified as amended at IOWA CODE § 542.4).

118. IOWA CODE § 542.4 (1981).

119. *See* Testimony of Neil Hamilton, *supra* note 59, at 4.

120. Testimony of Curt Sorteberg, Assistant to the President of the Iowa Farmers Union, to the Iowa Grain Elevator and Grain Grading Joint Subcommittee, at 2 (Aug. 19, 1980) (on file with the *Iowa Law Review*).

121. *See Hearings, supra* note 4, at 36 (statement of Pat Roberts, U.S. Representative from Kansas); Des Moines Register, Feb. 24, 1980, at 2F, col. 5 (quoting Maurice Van Nostrand, former Chairman of the Iowa Commerce Commission).

The cost to a grain dealer of each $1000 of bonding protection is approximately $10, or 1% of the value of the grain protected. *See* Letter from Paul H. Strayer, Assistant Vice President, AID Insurance Company (Mutual), to Thomas R. Zinkula (Sept. 22, 1982) (on file with the *Iowa Law Review*) (AID obtains its bonding rates from The Surety Association of America). If full bonding were required, 1% becomes a significant amount of money because the average grain elevator only achieves a return on sales of approximately 1.5%. J. Siebert, Financial Performance of Country Elevators 4-5 (Sept. 1980) (Cooperative Extension Service, Purdue University, No. EC-516).

122. If the goal is to provide complete protection to grain producers in the most cost-efficient way, a supplement to the bonding provision, such as an indemnity fund provision, should be considered. *See* Testimony of Neil Hamilton, *supra* note 59, at 4, 7. For an examination of the indemnity fund proposal, see text accompanying notes 184-202 *infra*.

Although the cost to grain dealers of bonds covering the total dollar amount of grain purchased by the dealers would be exorbitant, the legislature could make the amount of the mandatory bond proportional to the amount of grain purchased by each grain dealer, rather than fixing a set amount for each of the two classes.[123] A proportional bond would be more fair to grain dealers near the bottom of the two classes because they would not have to pay for bonds of the same amount as dealers near the top of the classes. A proportional bond also would be more fair to grain producers because, in the event of a grain dealer bankruptcy, grain dealers near the top of the classes would be more likely to sustain greater losses than dealers near the bottom. Yet, because the amount provided by bonds under the current bonding provision would be the same whether a bankrupt grain dealer was near the top or bottom of a particular class, grain producers would recover less per capita from the bonds of a bankrupt grain dealer near the top of a class.

Many states with grain dealer legislation already have proportional bonding provisions.[124] In general, these bonding provisions establish maximum and minimum bonds[125] and require a grain dealer to file a bond equal to a fixed percentage of the aggregate dollar amount paid by the dealer to producers for grain purchased from them during the dealer's last fiscal year.[126] It is recommended that the Iowa Legislature consider amending Iowa's grain dealer statute to change the current bonding provision to a proportional bonding provision similar to that of other states.

The 1981 amendment to the Iowa grain dealer statute also strengthened a second preexisting provision, the inspection provision, which is a post-license preventive provision. The major alteration that the legislature made in the inspection provision was the addition of a requirement that each grain dealer's premises, books, and records be inspected by the Iowa Commerce Commission at least once during each twelve-month period.[127] Prior to the amendment, the grain dealer statute contained only a discretionary inspection scheme.[128] A good inspection program is one of the most important preventive provisions of a successful grain dealer statute because the inspection of premises, books, and records

123. For a discussion of the Iowa grain dealer statute's two-class licensing system, see text accompanying notes 91-95 *supra*.

124. *E.g.*, Act of Aug. 21, 1967, § 3, ILL. REV. STAT. ch. 111, ¶ 303 (1979); MO. REV. STAT. § 276.436 (Supp. 1981).

125. For example, the Illinois maximum and minimum are $100,000 and $25,000, respectively. Act of Aug. 21, 1967, § 3, ILL. REV. STAT. ch. 111, ¶ 303 (1979). The Missouri maximum is $150,000, while the minimum is $20,000. MO. REV. STAT. § 276.436(1) (Supp. 1981).

126. For example, the Illinois percentage is 10%, Act of Aug. 21, 1967, § 3, ILL. REV. STAT. ch. 111, ¶ 303 (1979), and the Missouri percentage is 1%, MO. REV. STAT. § 276.436(2) (Supp. 1981).

127. Act of June 13, 1981, ch. 180, § 10, 1981 Iowa Acts 564, 569 (to be codified as amended at IOWA CODE § 542.9).

128. *See* IOWA CODE § 542.9 (1981).

is the best means of maintaining regular surveillance of licensees.[129] Because inspections are so important, a mandatory inspection provision is preferable to a discretionary provision.[130]

To carry out its mandatory inspection program effectively, the Iowa Commerce Commission needs a group of inspectors that is adequate in both quantity and quality.[131] The Iowa legislative subcommittee that investigated the grain elevator bankruptcy problem and proposed the 1981 amendment recognized the need for more inspectors.[132] Realizing that the state did not have enough money to hire more inspectors at that time,[133] the subcommittee recommended that license and inspection fees be increased to offset the cost of the additional inspectors' salaries.[134] The legislature followed that recommendation and included a provision in the 1981 amendment that increased license and inspection fees.[135] Therefore, grain dealer inspection programs are self-funded to a certain extent.

The subcommittee also considered the need for qualified inspectors.[136] It recognized that increasing the salaries paid by the state to inspectors was one way for the Iowa Commerce Commission to attract and retain qualified inspectors.[137] Moreover, the subcommittee recommended that the Commission should begin an apprenticeship program to train its new inspectors.[138] Whether a state inspection provision provides for mandatory or discretionary inspections, the adequacy of inspection personnel is a factor that the legislature cannot overlook if sound grain dealer legislation is desired.

The penalty provision of the Iowa grain dealer statute is a third previously existing provision strengthened by the 1981 amendment. The penalty provision can be classified as a preventive provision[139] because the threat of imprisonment may produce a strong deterrent effect on grain dealers who contemplate fraudulent violation of the grain dealer statute.[140] In the 1981 amendment the legislature increased the offense for a viola-

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129. *See* Iowa Grain Elevator and Grain Grading Joint Subcommittee of the Senate and House Committees on Agriculture and Commerce, Final Report to the Iowa General Assembly 9 (Jan. 1981) [hereinafter cited as Final Report].

130. *See id.*

131. *See* Iowa Grain Warehouse and Grain Grading Joint Subcommittee of the Committees on Commerce, Minutes 6 (Oct. 15, 1980).

132. *See id.* At that time Iowa had only 11 grain elevator inspectors, while Illinois had 36. WALLACES FARMER, Nov. 8, 1980, at 16.

133. Des Moines Register, Sept. 19, 1980, at 4A, col. 1 (quoting Iowa Senator Edgan Holden).

134. *See* Final Report, *supra* note 129, at 9-10.

135. Act of June 13, 1981, ch. 180, § 7, 1981 Iowa Acts 564, 568 (to be codified as temporarily amended at IOWA CODE § 542.6).

136. *See* Iowa Grain Warehouse and Grain Grading Joint Subcommittee of the Committees on Commerce, Minutes 6 (Oct. 15, 1980).

137. *See id.*

138. Final Report, *supra* note 129, at 9.

139. *See* Testimony of Neil Hamilton, *supra* note 59, at 5.

140. GRAIN ELEVATOR TASK FORCE, *supra* note 18, at 27.

tion of the grain dealer licensing laws to a serious misdemeanor for some violations and an aggravated misdemeanor for others.[141] These changes will increase the number of prosecutions and, thus, arguably increase deterrence because, while prosecutors tend not to commit the time and resources necessary to prosecute cases in which violations are treated as simple misdemeanors, they are more likely to prosecute serious or aggravated misdemeanors.[142]

V. POTENTIAL AMENDMENTS TO THE IOWA GRAIN DEALER STATUTE

While current Iowa Code preventive provisions attempt to control many of the causes of grain dealer bankruptcies, there are two major causes that the legislative provisions do not address: delayed pricing[143] and speculation.[144] Moreover, while the remedial bonding provision provides grain producers with some compensation in the event of a grain dealer bankruptcy, it cannot provide total protection.[145] Because of these deficiencies in the Iowa law, it is necessary to examine potential amendments to the grain dealer statute.[146]

A. Delayed Pricing and Speculation Controls

Delayed pricing[147] is a major cause—perhaps the major cause—of

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141. Act of June 13, 1981, ch. 180, § 11, 1981 Iowa Acts 564, 570 (to be codified as amended at IOWA CODE § 542.11(2)). The statute provides:

> A person who engages in business as a grain dealer without obtaining a license, or who refuses to permit inspection of licensed premises, or books, accounts, records, or other documents required by this chapter, or who uses a scale ticket, or credit-sale contract that fails to satisfy requirements established by the commission commits a serious misdemeanor, except that a person who commits any of these offenses after having been found guilty of the same offense commits an aggravated misdemeanor.

Id., 1981 Iowa Acts at 570. All other violations remain simple misdemeanors. *Id.*, 1981 Iowa Acts at 570 (to be codified as amended at IOWA CODE § 542.11(3)). Also, injunctions may be issued against grain dealers who are in violation of the statute. *Id.*, 1981 Iowa Acts at 570 (to be codified as amended at IOWA CODE § 542.11(4)).

142. Final Report, *supra* note 129, at 8.

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

144. *See* note 77 *supra* and accompanying text.

145. *See* text accompanying notes 119-22 *supra*.

146. A potential remedial addition to the Iowa Code that will not be discussed further in this Note concerns the possibility of amending Iowa's Uniform Commercial Code provisions. A major problem faced by grain producers when a grain dealer goes bankrupt is the producers' low priority with respect to the grain assets of the dealer. *See* text accompanying note 153 *infra*. The Iowa Legislature might consider adopting a proposal similar to a new Illinois statute, which would help solve that problem. The new Illinois statute creates a statutory lien on the grain assets of a bankrupt elevator in favor of grain producers who have written evidence of ownership that discloses storage obligations of the elevator or written evidence of sale of grain to the elevator. The statute gives grain producers a priority position with respect to the grain assets. *See* Act of June 29, 1982, Pub. Act 82-771, 1982 Ill. Legis. Serv. 230 (West).

147. For other phrases commonly used to describe delayed pricing, see note 79 *supra*.

grain elevator bankruptcies,[148] but it is not addressed directly by any provision of the Iowa grain dealer statute. Delayed pricing occurs when a grain dealer receives grain subject to a condition that the price will be established at a later date.[149] The date of pricing is the choice of the grain producer but must be within a time period agreed on by the grain dealer and the grain producer. The price is usually the grain dealer's bid price on the actual day of pricing, minus accrued service charges.[150] The problem with delayed pricing is that it encourages speculation because the grain dealer has title to the grain and, therefore, can sell it and use the money to purchase futures contracts.[151] The problem often manifests itself during the bankruptcy proceedings that are the aftermath of improvident speculation, wherein the dealer has purchased futures contracts at a high price and has been forced to sell the contracts for a low price.[152] Because the grain producers who sold grain on a delayed-pricing basis lost title to the grain as soon as they delivered it to the grain dealer, they must file a claim and stand in line with all the other unsecured creditors if the elevator becomes bankrupt.[153]

One possible solution to the problems caused by delayed pricing is to outlaw the use of delayed-pricing contracts altogether. However, because of the value of delayed pricing, banning its use should be the last resort.[154] Delayed pricing is attractive to grain producers because it allows effective ownership of grain beyond available storage capacity and, thereby, permits the producers to engage in price level speculation on larger quan-

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148. Des Moines Register, Feb. 24, 1980, at 2F, col. 5.

149. D. Good, Delayed Pricing by Country Elevators 1 (Sept. 1977) (Illinois Agricultural Economics Staff Paper, University of Illinois, Urbana-Champaign, No. 77 E-22).

Delayed-pricing contracts should not be confused with delayed-payment contracts. In a delayed-payment contract, all the terms of the sale are set, including price. However, payment is to be made at a later date, generally for tax purposes. WALLACES FARMER, Oct. 24, 1981, at 9.

The Prairie Grain Company may have collapsed because the owner lost a considerable amount of money speculating in the futures market. *See* Des Moines Register, Feb. 17, 1980, at 1A, col. 1. Delayed-pricing arrangements were blamed for encouraging the speculation. *Hearings, supra* note 4, at 150 (statement of Reuben L. Johnson, Director of Legislative Services, National Farmers Union).

150. D. Good, Delayed Pricing by Country Elevators 1 (Sept. 1977) (Illinois Agricultural Economics Staff Paper, University of Illinois, Urbana-Champaign, No. 77 E-22).

151. *See* Zarley, *Delayed Price Contracts: Half-Breed with Pitfalls,* SUCCESSFUL FARMING, Aug. 1980, at 17.

152. *See* L. UCHTMANN, J. LOONEY, N. KRAUSZ & H. HANNAH, AGRICULTURAL LAW: PRINCIPLES AND CASES § 12.5, at 416-17 (1981).

153. *See* U.C.C. § 9-301(1)(a) (1978); *see also* Looney & Byrd, *Protecting the Farmer in Grain Marketing Transactions,* 31 DRAKE L. REV. 519, 520-21 (1981-82); Zarley, *Delayed Price Contracts: Half-Breed with Pitfalls,* SUCCESSFUL FARMING, Aug. 1980, at 17.

154. *See* Zarley, *Delayed Price Contracts: Half-Breed with Pitfalls,* SUCCESSFUL FARMING, Aug. 1980, at 17 (quoting former Iowa Commerce Commission Chairman Maurice Van Nostrand).

It is estimated that 10% to 15% of all sales to grain elevators are by delayed-pricing contracts. Iowa Grain Warehouse and Grain Grading Joint Subcommittee of the Committees on Commerce, Minutes 14 (Aug. 19, 1980).

tities of grain after they have finished marketing it.[155] Delayed pricing is also valued by grain dealers because it gives them access to grain sooner than producers may want to relinquish ownership.[156] Because grain dealers get title to the grain and may dispose of it as they see fit, they conceivably can do a better job of grain merchandising.[157]

The use of delayed pricing by grain dealers can be divided into four major categories.[158] First, delayed pricing can be used by grain dealers as a substitute for storage. The reason for this use of delayed pricing is inadequate storage space.[159] Second, delayed pricing often is used in connection with ground-stored grain because it allows the producer to retain effective ownership of grain but, at the same time, holds the dealer responsible for the quality of the grain.[160] Third, because the dealer has control of the grain, it can take advantage of unusually good selling opportunities as they occur during the marketing season.[161] Fourth, delayed pricing allows the dealer to move producer-owned grain out of storage. That flexibility is important when the dealer approaches harvest of a new crop with higher than desirable levels of the old crop in its storage facilities.[162]

Despite the usefulness of delayed pricing to grain producers and dealers, it has pitfalls that legislation possibly could control. Problems arise because grain dealers can sell the grain that they have title to via delayed-pricing contracts and use the proceeds in whatever ways they desire.[163] Therefore, although the proceeds from the sale of the grain rightfully belong to the grain producers, or at least will belong to the grain producers in the future, grain dealers are able to use the money for speculation on the board of trade or in unwise investments.[164] A few states protect grain producers who sell their grain by means of delayed-pricing contracts by requiring each grain dealer to establish an escrow account containing specified liquid assets to cover a fixed percentage of delayed-pricing obligations owed by the dealer to producers.[165] The purpose of escrow account requirements is to assure that grain dealers who purchase grain on a delayed-pricing

155. D. Good, Delayed Pricing by Country Elevators 1 (Sept. 1977) (Illinois Agricultural Economics Staff Paper, University of Illinois, Urbana-Champaign, No. 77 E-22).

156. *Id.* at 1-2.

157. *Id.* at 2.

158. *Id.* at 8.

159. *Id.* at 8-10.

160. *Id.* at 10.

161. *Id.* at 11.

162. *Id.* at 12. The extent of the usefulness of delayed pricing in these four major categories is questionable, however, and delayed pricing may not be the treasure that some grain dealers might think it is. Unfortunately, delayed pricing is often used when better alternatives exist. *See id.* at 8-13.

163. *Hearings, supra* note 4, at 41 (statement of John R. Block, U.S. Secretary of Agriculture).

164. *Id.*

165. *See, e.g.*, Act of Aug. 21, 1967, § 10, ILL. REV. STAT. ch. 111, ¶ 311 (1979); MICH. COMP. LAWS § 285.67a (Supp. 1982-83).

basis will maintain solvent business positions, thus enabling them to satisfy their delayed-pricing obligations to grain producers.[166]

To understand the utility of an escrow account requirement, it is helpful to examine how a statutory provision that institutes an escrow account might work. Illinois' escrow account provision provides a model example.[167] Under the Illinois scheme, ninety percent[168] of a grain dealer's obligations for grain purchased by delayed pricing must be evidenced by one or more of the following liquid assets: grain, rights in grain, or proceeds of grain.[169] The Illinois statute also requires each grain dealer to practice an effective method of price protection, such as the procurement of options on a licensed commodity exchange.[170] This escrow account provision, added to the Illinois grain dealer statute in direct response to major failures of Illinois grain dealers,[171] may have helped achieve beneficial results in Illinois. Since the revision of its grain dealer law, no more than one Illinois grain dealer has failed each year.[172] Because delayed pricing is a major cause of grain dealer failures,[173] and an operative legislative remedy aimed directly at delayed-pricing pitfalls is available, the Iowa Legislature should consider adopting an escrow account provision similar to that existing in other states.[174]

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166. *See* Final Report, *supra* note 129, at 8.

167. The Iowa legislative subcommittee that examined the problem of grain elevator failures recommended that the legislature adopt an escrow account provision similar to the requirements imposed on grain dealers by Illinois law. *Id.* at 7-8. The subcommittee included a similar provision in its legislative proposal. *Id.* at 1-3 (pages refer to those of the proposal, which follows the final report). However, the legislature did not include an escrow account provision in the enacted bill.

168. The comparable figure in Michigan is "not less than 50%." MICH. COMP. LAWS § 285.67a(d) (Supp. 1982-83). The Iowa subcommittee that recommended the adoption of an escrow account provision suggested a figure of 80%. Final Report, *supra* note 129, at 2 (page refers to that in proposal). The higher the percentage of grain that is required to be evidenced in an escrow account, the more complete the protection is for grain producers.

169. Act of Aug. 21, 1967, § 10, ILL. REV STAT ch. 111, ¶ 311 (1979).

The phrase "rights in grain" refers to warehouse receipts issued to the grain dealer by licensed warehouses. *Id.* § 10(B), ILL. REV. STAT. ch. 111, ¶ 311(B). The phrase "proceeds of grain" includes cash, short-term investments held in licensed financial institutions, balances on grain margin accounts, delayed-pricing contracts for grain shipped to terminals, and other proceeds acceptable to the regulatory agency. *Id.* § 10(C), ILL. REV STAT ch. 111, ¶ 311(C).

170. *Id.* § 10, ILL. REV STAT ch. 111, ¶ 311.

171. *See Hearings, supra* note 4, at 41 (statement of John R. Block, U.S. Secretary of Agriculture).

172. FARM J., June-July 1980, at 60.

173. *See* Des Moines Register, Feb. 24, 1980, at 2F, col. 5 (quoting Maurice Van Nostrand, former Chairman of the Iowa Commerce Commission and a former grain elevator operator).

174. Another suggestion for alleviating the problems caused by delayed pricing is to replace the current delayed-pricing system with what is referred to as the "seller's call," which is a futures-based, delayed-pricing program. Clark, *Stockport: What Might Have Been,*

Speculation in the futures market is the other major cause of grain dealer bankruptcies[175] that the Iowa grain dealer statute does not address directly. Although there is a connection between delayed pricing and speculation, the proceeds obtained by a grain dealer from the sale of delayed-price grain is only part of the money the dealer might lose because of improvident speculation in the futures market. Therefore, the speculation now under consideration is that which occurs whether or not the grain dealer is involved in delayed pricing.[176]

Grain dealers arguably have to use the futures market to stay in business. The volatile nature of the market encourages grain dealers to seek the protection afforded by hedges on the futures market.[177] However, it is submitted that minimal controls on speculation by grain dealers may reduce the number of bankruptcies that result when the speculation is excessive.[178] Once again, Illinois requirements provide guidance. The Illinois grain dealer statute permits the regulatory agency, the Illinois Department of Agriculture,[179] to establish speculation limits.[180] The Department bases speculation limits on the net worth of grain dealer businesses.[181]

Des Moines Register, Mar. 15, 1980, at 12A, cols. 3-6. Under a "seller's call" system, instead of relying on an individual grain dealer to effect a future sale of entrusted grain, the grain producer could immediately sell his grain to the dealer. The producer would ordinarily specify the sales price formula at the time of sale, in terms of a specified discount from the controlling Chicago futures price. Later, the producer could specify the exact day on which the current futures quotation would be plugged into the formula to fix the sum that the dealer would have to remit to the producer. *Id.*

175. *Hearings, supra* note 4, at 70, 77 (report of the Illinois Legislative Council).

176. Grain dealers enter into the commodity futures markets either as speculators or as hedgers. *See generally* 1 J. DAVIDSON, AGRICULTURAL LAW §§ 5.09-.11 (1981). Speculators assume the risk of price fluctuations in exchange for potential gains in the market. They buy futures when they think the market will rise and sell when they think it will fall. *Id.* § 5.11, at 391. Hedgers are risk shifters. They have an interest in the underlying physical commodity and attempt to counterbalance their market commitments to avoid or lessen financial loss. *See id.* § 5.10, at 390. Generally, grain dealers are concerned about the possibility of price declines so they execute selling hedges by selling enough futures to offset their cash positions. *See* Clark, *Stockport: What Might Have Been,* Des Moines Register, Mar. 15, 1980, at 12A, cols. 3-6. Futures trading has been fully discussed in other texts. *See generally* T. HIERONYMUS, ECONOMICS OF FUTURES TRADING (1971); F. HORN & V. FARAH, TRADING IN COMMODITY FUTURES (2d ed. 1979).

177. Des Moines Register, Feb. 24, 1980, at 2F, col. 3 (quoting Jim Higgs, manager of the Farmers Co-op Elevator, Waukee, Iowa).

178. The Iowa legislative subcommittee that examined the grain elevator problem also thought that speculation should be regulated, Final Report, *supra* note 129, at 9, and included a section dealing with the regulation of speculation in its legislative proposal, *id.* at 10 (page refers to that in proposal accompanying final report).

179. Act of Aug. 21, 1967, § 1, ILL. REV. STAT ch. 111, ¶ 301 (1979).

180. *See id.* §§ 6, 7, ILL. REV. STAT. ch. 111, ¶¶ 306, 308. Regulation 3.04 states: "No license shall be issued to any applicant who fails to complete the submission of all license requirements within five months of the date of the applicant's financial statement." Rules and Regulations for "The Grain Dealers Act," 3 Ill. Admin. Reg. no. 19, at 3 (adopted May 11, 1979) (to be codified at 68 ILL. ADMIN. CODE ch. II, § 600.30(d)).

181. *See* Letter from James H. Onken, Bureau Chief, Bureau of Warehouses, Illinois

Each grain dealer licensee is allowed a position of long or short grain, on which the dealer is subject to the risk of price fluctuation, at the rate of one bushel for each ten dollars in net worth for the major commodity handled, with a minimum of 5000 bushels and a maximum of 50,000 bushels. Each licensee is also allowed to speculate on one-half bushel for each ten dollars in net worth for each of every other commodity handled, with a minimum of 5000 bushels and a maximum of 25,000 bushels.[182] For example, a grain dealer with a net worth of $250,000 can be in a speculative position in the futures market on 25,000 bushels of corn and 12,500 bushels of other grains. Given the significant role excessive speculation plays in causing grain dealer bankruptcies,[183] the Iowa Legislature should consider imposing similar controls on speculation by Iowa grain dealers.

B. An Indemnity Fund Proposal

Currently, the Iowa grain dealer statute has only one remedial provision, the bonding provision, that provides grain producers with compensation for the losses they sustain after a grain dealer bankruptcy due to the failure of preventive statutory provisions. However, the mandatory bond usually cannot provide the grain producers with total compensation.[184] Therefore, because total compensation should be the goal of a remedial program,[185] other remedial provisions need to be considered.

In recent years a number of states have considered creating some form of an indemnity fund, the money from which would be available to compensate grain producers who suffer losses within the grain handling system.[186] The indemnity fund could be patterned after the Federal Deposit Insurance Corporation (FDIC) for bank customers[187] and the Client Security Trust Fund for the clients of Iowa attorneys.[188] A few state legis-

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Department of Agriculture, to all Grain Dealers (June 24, 1980) (on file with the *Iowa Law Review*).

182. *Id.*

183. *See* note 77 *supra* and accompanying text.

184. *See* text accompanying notes 119-22 *supra.*

185. Testimony of Neil Hamilton, *supra* note 59, at 4.

186. *See, e.g., Hearings, supra* note 4, at 42 (statement of John R. Block, U.S. Secretary of Agriculture and former Illinois Secretary of Agriculture) (Illinois); *id.* at 52 (statement of Robert T. Stephan, Kansas Attorney General) (Kansas); Testimony of Neil Hamilton, *supra* note 59, at 8 (Ohio). Even the United States Congress has considered enacting a federal grain insurance program for grain producers. *Hearings, supra* note 4, at 39 (statement of Dan Glickman, U.S. Representative from Kansas).

187. *See* FARM J., May 1981, at 48. The FDIC insures the deposits of all banks that are entitled to the benefits of insurance. 12 U.S.C. § 1811 (1976). Money for the fund comes from assessments from insured banks. *See id.* § 1817. The maximum amount of the insured deposit of any depositor is $100,000. *Id.* § 1821(a)(1) (1976 & Supp. IV 1980).

188. *See* Letter from David P. Miller, President and Owner of Batavia Grain, Inc., to the Iowa Grain Elevator and Grain Grading Joint Subcommittee, at 2 (Aug. 19, 1980) (on file with the *Iowa Law Review*). On December 5, 1973, the Iowa Supreme Court adopted Rule 121, *see* IOWA CT R. 121, which created the Client Security and Attorney Disciplinary

latures have already adopted provisions establishing indemnity funds.[189] Iowa has considered establishing an indemnity fund for several years[190] and came close to doing so in 1981;[191] however, supporters of the fund have failed to gain the backing necessary to pass their proposed bills into law.

The indemnity fund proposal that was part of the 1981 Iowa grain elevator bill until removed by amendment[192] was particularly well drafted. Under the defeated proposal, grain producers would have had to have voted in favor of establishing the fund, in a referendum held for that purpose, before the funding mechanism could be set into motion.[193] If the indemnity fund were supported by a majority of Iowa grain producers, the producers would then be assessed one-tenth of one cent for every dollar of value of grain delivered by a grain producer to a grain handler for storage or sold by the producer to the handler.[194] The assessment period

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Commission. *Id.* R. 121.1(a). The Commission has the duty to administer and operate the Clients' Security Trust Fund of the Bar of Iowa, *id.* R. 121.1(b), which also was created by the Iowa Supreme Court's adoption of Rule 121, *see id.* R. 121.3(a). The purpose of the fund is "to prevent defalcations by members of the Iowa bar, and insofar as practicable, to provide for the indemnification by the profession for losses caused to the public by the dishonest conduct of members of the bar of this state." *Id.* R. 121.3(c). Money for the fund is collected from Iowa attorneys through a system of annual assessments. *See id.* R. 121.3(i). As of November 30, 1981, the balance in the fund was $1,096,735. IOWA CLIENT SECURITY & ATTORNEY DISCIPLINARY COMM'N, 1981 ANNUAL REPORT 1.

189. Maryland established an indemnity fund of $5,000,000 through the assessment of one-half cent per bushel on all grain delivered by grain producers to grain buyers. MD. AGRIC. CODE ANN. §§ 13-101 to -108 (Supp. 1981).

Oklahoma has a fund of $10,000,000, the money for which comes from a levy of two-tenths of a cent per bushel. OKLA. STAT. tit. 2, §§ 9-41 to -47 (1981).

South Carolina's $3,000,000 fund is financed through the assessment of one cent per bushel on soybeans and one-half cent per bushel on other grains. S.C. CODE ANN. § 39-21-310 (Law. Co-op. Supp. 1981).

190. Testimony of Neil Hamilton, *supra* note 59, at 7.

191. *See* Des Moines Register, May 2, 1981, at 9A, cols. 1-2.

192. *Id.* Many legislators thought that, without the indemnity fund provision, the grain elevator bill did not provide grain producers with much protection against elevators that fail. *Id.*

193. H.J. 841 amend. H-3948, 69th G.A., Extraordinary Sess. 1603, 1607-08 (May 4, 1981).

194. *Id.* at 1604.

In 1980 Iowa grain producers produced corn worth $4,608,450,000, UNITED STATES DEP'T OF AGRICULTURE, 1981 AGRICULTURAL STATISTICS 34, and soybeans worth $2,402,849,000, *id.* at 132, for a total of $7,011,299,000. Therefore, if that rate of production continued in future years, and if only one-tenth of one cent for every dollar of value were assessed for indemnity fund purposes, it would take less than one and one-half years to accumulate the $10,000,000 indemnity fund, assuming all the grain produced in Iowa is either stored at or sold to grain elevators. However, because some grain is stored or used by the producers themselves and, therefore, not assessed for the purposes of the fund, it would actually take somewhat longer than one and one-half years to collect the money for the fund. See note 189 *supra* for assessment rates in states with indemnity funds. Soybeans could be assessed at a higher rate than corn because of their greater value per bushel.

would continue until the fund reached $10,000,000.[195] Once the fund was established, grain producers who incurred losses in connection with the storage or sale of grain would be entitled to compensation from the fund of eighty percent of their losses.[196] In exchange for compensation from the fund, grain producers would have to assign to the state their rights to proceeds from bonds, insurance policies, and bankruptcy settlements.[197] Whenever the balance in the fund dropped below $7,500,000, assessments would begin anew in order to replenish the fund.[198]

There is a difference of opinion among Iowans who are associated with the grain industry concerning the merits of an indemnity fund. While the majority of Iowa legislators do not support the establishment of an indemnity fund, evidence suggests that the majority of Iowa farmers do. Of the 238 Iowa farmers polled in a 1981 survey, sixty-one percent favored an indemnity fund.[199] It is significant that farmers are in favor of an indemnity fund because farmers probably would be responsible for funding it.[200]

A frequently expressed argument against the establishment of an indemnity fund is that it would lead grain producers to think that the fund gave them full protection, and they perhaps might then neglect to exercise caution in their grain transactions.[201] However, the eighty percent recovery of losses provision of the 1981 Iowa indemnity fund proposal reduces the force of the argument concerning neglected caution. Even if the proposed fund were implemented, grain producers presumably would exercise caution in dealing with grain handlers because they would recover only eighty percent of their grain transaction losses. Furthermore, supporters of an indemnity fund argue that, beyond providing remedial relief

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195. H.J. 841 amend. H-3948, 69th G.A., Extraordinary Sess. 1603, 1604 (May 4, 1981).

If the Iowa Legislature adopts the indemnity fund idea, it should also consider whether a $10,000,000 fund is large enough. One big grain elevator failure like the Prairie Grain failure, which resulted in grain losses to producers of over $6,000,000, *see* text accompanying note 4 *supra*, would drain the fund significantly, even if the producers recovered only 80% of their losses, *see* text accompanying note 196 *infra*.

196. H.J. 841 amend. H-3948, 69th G.A., Extraordinary Sess. 1603, 1605-06 (May 4, 1981).

197. *Id.* at 1606.

198. *Id.* at 1604.

199. WALLACES FARMER, Apr. 11, 1981, at 20. Twenty percent of those questioned in the *Wallaces Farmer* poll were opposed to an indemnity fund, and nineteen percent were undecided. *Id.*

200. Fifty-seven percent of the Iowa farmers favoring an indemnity fund in the *Wallaces Farmer* poll thought that grain producers and grain elevators should share the responsibility for funding the fund. Ten percent thought that producers should support the fund entirely; twenty percent wanted it to be funded solely by grain elevators; and thirteen percent were undecided. *Id.* However, it is arguable that if grain elevators were responsible for funding the fund, they would ultimately pass the cost on to grain producers in the form of lower prices. Des Moines Register, Nov. 18, 1980, at 3A, col. 1.

201. *See, e.g.*, Final Report, *supra* note 129, at 7; Des Moines Register, Dec. 12, 1980, at 4A, col. 3 (quoting delegates to the Iowa Farm Bureau Federation convention).

to grain producers who suffer grain transaction losses, the fund would provide an additional benefit: the interest earned on the $10,000,000 fund could be used to hire more grain elevator inspectors,[202] thereby increasing the overall strength of preventive regulations.

C. The Limits of Existing and Proposed Legislation

All the proposed legislation and all the current Iowa grain dealer provisions examined in this Note are, to some degree, efficacious in preventing grain dealer bankruptcies or compensating grain producers for losses that do occur. However, it is not suggested that all the proposals should be enacted hastily into law or that all the current legislative provisions should remain law without question. Before any legislative decisions are made, solutions to the grain dealer bankruptcy problem should be evaluated in terms of the adverse effects of regulations on the grain marketing system.[203] The cost of excessive and stiff regulations might force some small, though financially solid, grain dealers out of business.[204] Moreover, even if all the grain dealers remained in business, most of the cost of excessive and stiff regulations eventually would be borne by grain producers, who are intended to be the beneficiaries of increased regulation.[205] Therefore, a thorough cost-benefit analysis should be conducted concerning the effectiveness and efficiency of legislative remedies.

Existing Iowa Code grain dealer provisions and proposed alternatives, improvements, or additions should be analyzed. The first step of such an analysis would be to determine the benefits of completely effective grain dealer legislation, by measuring the total costs to grain producers of grain dealer bankruptcies, which the legislation would aim to eliminate.[206] Next, the potential costs and benefits of each legislative provision and proposal to grain producers, grain dealers, and the state of Iowa would be assessed.[207] The final step would be to compare the costs and benefits of the various legislative provisions and proposals to one another and to the total cost of grain dealer bankruptcies incurred by Iowa grain producers. The sug-

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202. Des Moines Register, Nov. 18, 1980, at 3A, col. 1.

203. *See* Iowa Grain Warehouse and Grain Grading Joint Subcommittee of the Committees on Commerce, Minutes 2 (Aug. 19, 1980) (testimony of Neil Hamilton, Assistant Attorney General in the Farm Division of the Office of the Iowa Attorney General).

204. WALLACES FARMER, Nov. 8, 1980, at 16; *see* Des Moines Register, Feb. 28, 1982, at 1F, cols. 5-6. Iowa Commerce Commission officials estimate that one-quarter of Iowa's 2000 licensed grain dealers surrendered their licenses in an eight month period following July 1981, when the new, tighter restrictions covering grain dealers went into effect. *Id.*

205. *See* Statement of Dean Kleckner, President of the Iowa Farm Bureau Federation, to the Iowa House Agriculture Committee, at 1 (Mar. 17, 1981) (regarding grain marketing) (on file with the *Iowa Law Review*).

206. *See generally* Keith, *Revolutionary Changes Being Considered in Government Warehouse Programs,* GOVERNMENT & GRAIN, Oct. 15, 1981, at 2-3.

207. *See generally* Keith, *USDA's Elevator Task Force Hangs Hat on CPA Audit,* GOVERNMENT & GRAIN, Sept. 10, 1981, at 3-4.

gested analysis would allow legislators to determine the optimal combination of legislative provisions and proposals.[208] Of course, the total costs of the optimal combination should be less than the total benefits.[209] Also, in comparing the provisions and proposals to one another, the most economical and effective provisions and proposals should be given priority.[210]

The most competent forum to make a cost-benefit analysis is the Iowa Legislature. Perhaps a subcommittee, similar to the subcommittee that worked on the 1981 amendment to the Iowa grain dealer statute, could be created to consider legislative alternatives in a cost-benefit fashion. It is not unfair to use the taxpayers' money to pay the costs of developing an optimal legislative regulatory program pertaining to grain dealers, because everyone—not only grain producers—suffers when grain elevators fail.[211] Moreover, grain producers will ultimately be responsible for the costs to the grain industry of complying with additional and more stringent regulations.[212]

VI. CONCLUSION

The number of grain elevator bankruptcies has been increasing significantly over the past few years, and the outlook for the future is even more discouraging. Grain producers and others suffer both direct and indirect economic losses as a result of grain elevator bankruptcies. To solve the problems that are caused by grain elevator failures, effective state legislation to regulate grain dealers is essential. Adequate preventive and remedial provisions are necessary.

A 1981 amendment to the Iowa grain dealer statute added new regulatory provisions and changed existing provisions. An examination of the recently amended grain dealer statute has shown that each regulatory provision confronts one or more of the causes of grain dealer failures. When considered separately, the advantages of each of the provisions outweigh their respective disadvantages.

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208. *See generally id.*

209. The conflicting interests that must be considered when a legislature is deciding on the type and extent of grain elevator regulations have been explained as follows:

> [I]n considering alternative approaches or improvements to existing laws, we must realize the importance of achieving a regulatory balance which offers protection to grain owners without being overly restrictive to the grain industry. We must consider measures which are practical, economical, and which compliment and assist the free enterprise system.

Hearings, supra note 4, at 66 (statement of Thomas D. Hopkins, Coordinator of the Grain Regulatory Services Program, Division of Grain Inspection and Warehousing, Missouri Department of Agriculture).

210. *See generally* Keith, *USDA's Elevator Task Force Hangs Hat on CPA Audit,* GOVERNMENT & GRAIN, Sept. 10, 1981, at 4.

211. *See* text accompanying notes 21-23, 31-42 *supra.*

212. *See* text accompanying notes 122, 200 *supra.*

The current Iowa grain dealer statute is far from perfect, however. It does not attempt to control delayed pricing or speculation, both of which are recognized as major causes of grain dealer failures. Also, the bonding provision of the existing statute provides grain producers with only a limited amount of compensation for the losses that they suffer as a result of grain dealer failures. The implementation of an indemnity fund provision could furnish an additional source of compensation for grain producers.

It is suggested that the Iowa Legislature examine the costs and benefits of the proposed improvements to the existing Iowa grain dealer legislation as well as the costs and benefits of the existing statutory provisions. The legislature's goal should be to ascertain the most cost-efficient combination of regulatory measures that will solve the problem of grain elevator failures without imposing undue burdens on the grain industry.

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