

Frequently Asked Questions about the PUC's H & I Grain insolvency docket

Aug. 2, 2017

What is the current status of H & I Grain as a grain buyer?

On July 21, 2017, the PUC revoked H & I Grain of Hetland's grain buyer license. This action affects all of H & I Grain's locations in Hetland, De Smet and Arlington, South Dakota. Prior to revocation, the PUC suspended H & I Grain's grain buyer license on June 23, 2017.

Why did the PUC take these actions – suspension then revocation of license – against H & I Grain?

PUC staff cited a number of known acts of insolvency when recommending to the commission that H & I Grain's license be suspended. These included draft financial statements that showed significant deficiencies in working capital and equity; notices of intent to sue on bond filed with the PUC by a number of producers; and grain producers being refused payment or re-delivery of their grain by H & I Grain.

Why are H & I Grain trucks still hauling grain?

H & I Grain had their grain buying license revoked by the PUC. The company can no longer purchase grain from producers. PUC staff recently received reports of activity at H & I Grain's De Smet and Hetland locations and looked into the situation, learning that H & I Trucking is hauling grain for hire for another grain buyer. H & I Grain officials and this particular grain buyer have been contacted by PUC staff. Staff learned this buyer is allowing H & I Grain to blend remaining out-of-condition bushels with good quality grain that buyer is hauling. H & I Grain is not purchasing grain. When the out-of-condition bushels are gone, H & I Grain officials have stated the company will no longer blend grain at its facilities. The transactions occurring are not in violation of the commission's order of revocation. PUC staff will continue to monitor the situation and will investigate any additional concerns that are reported to the PUC about activity at H & I Grain locations.

What is the total amount of losses producers may have sustained as a result of H & I Grain's insolvency?

PUC staff has estimated producer losses as the result of H & I Grain's insolvency to be in excess of \$7 million. However, there are a number of factors that could cause that figure to increase or decrease.

How and when did the PUC become aware of financial problems at H & I Grain?

On June 14, 2017, after numerous requests made to H & I Grain by PUC staff, the company submitted a draft balance sheet and income statement. Review of the documents led to further investigation by PUC staff that revealed H & I Grain had suffered significant financial losses. This information led PUC staff to request on June 19, 2017, that the PUC suspend H & I Grain's grain buyer license. PUC staff continued to conduct an investigation, relative to state law and administrative rules.

What did the PUC's investigation of H & I Grain reveal?

PUC staff completed a general investigation of H & I Grain in early July 2017. Based upon that investigation and information staff continues to uncover, open payables of H & I Grain are in excess of \$790,000. Also based on the investigation, PUC staff has good cause to believe that H & I Grain has priced later and deferred payment contracts totaling nearly \$6.5 million.

What communication did the PUC have with H & I Grain prior to the investigation that led to the company's license being suspended?

On June 2, 2016, H & I Grain submitted its application to the PUC for renewal of its grain buyer license along with the company's fiscal year 2015 reviewed financial statements. Based on the financial statements submitted

by H & I Grain, the company met the licensing requirements in state law and a grain buyer's license was issued on June 9, 2016, for the period of July 1, 2016, through June 30, 2017.

On Oct. 27, 2016, PUC staff traveled to H & I Grain's locations in Hetland, De Smet and Arlington to investigate a report about out-of-condition grain. PUC staff questioned H & I Grain personnel, who stated out-of-condition grain had been blended and marketed and that the situation did not create a financial hardship for the company. PUC staff was in contact with H & I Grain five times between Oct. 27, 2016 and June 13, 2017, to request the company submit its fiscal 2016 financial statements. PUC staff's requests were met with either no response or a reply that the requested reports were not yet available. Renewal documents were not submitted to the PUC by H & I Grain for the July 1, 2017, through June 30, 2018, licensing period. PUC staff conducted inspections at H & I Grain in July, August and October 2016, and in April and May 2017.

Why didn't PUC inspections reveal the H & I Grain financial problem sooner?

The key indicator of a solvency problem with a grain buyer is late payables. Grain producers typically alert the commission when they are having problems getting paid for grain that has been delivered to a buyer. The PUC did not receive any complaints of slow pay. Based on the investigation, PUC staff has reason to believe that H & I Grain officials may have concealed aging open payables by preparing settlement and assembly sheets and drafting checks that they did not mail to farmers. The checks were placed in a file and held in the H & I Grain office. When PUC inspectors examined the books during inspections, these accounts appeared as settled accounts when in reality, the producer was not being paid.

Additionally, South Dakota law requires grain buyers and grain warehouses to notify the PUC if they fall out of compliance with any of the financial licensing requirements. Failure to report non-compliance with financial licensing requirements is a criminal offense. At no time during the 2016-2017 licensing period did H & I Grain contact the PUC to report they were out of compliance.

South Dakota law requires grain buyers to allow PUC inspectors full access to prepared financial records. The law requires a grain buyer to prepare financial statements for their fiscal year-end and to submit them with their application at renewal. The PUC does not have legal authority to compel a grain buyer to prepare and submit monthly or quarterly balance sheets if they are not doing them through their regular course of business.

How often are grain buyers inspected by the PUC? How many inspectors are there and what do they inspect?

Each licensed grain facility must receive one inspection each year according to state law. However, the current PUC inspection process typically results in each facility being inspected once every six to nine months. When the commission receives reports of slow pay or other concerns with a licensed facility, additional inspections are conducted to investigate. The staff will also communicate with the facility's owners and management team, as was done in the H & I Grain matter. Two full-time grain warehouse inspectors work for the commission, performing inspections at the approximately 270 licensed grain buying and warehouse facilities statewide.

Will the PUC take receivership of H & I Grain?

The PUC will not seek receivership of H & I Grain. The investigation by PUC staff showed that the assets of H & I Grain are fully encumbered. A receivership initiated by the PUC would be at significant expense to South Dakota taxpayers, and the only perceived beneficiary of a receivership would be the secured creditor, H & I Grain's bank.

Does H & I Grain have a bond?

As part of the licensing process, H & I Grain was required to post a surety bond in the amount of \$400,000. The bond was issued by North American Specialty Insurance Co.

What determines the amount of the bond?

The bond level is established by state law. Bond amounts are determined during the licensing and license renewal period according to [SDCL 49-45-9](#) and are based on average purchases over a three-year period. In accordance with the bond requirement statute, H & I Grain was bonded at \$400,000.

What is the process for customers of H & I Grain who have not been paid to collect on the bond?

PUC staff completed an examination of H & I Grain's scale tickets to determine the customers that sold grain to H & I Grain but did not receive payment. The PUC sent notice to these customers via certified mail on July 21, 2017. The PUC also published notice of revocation in several area newspapers. Those that have a valid claim to the bond must file with the PUC by Jan. 24, 2018. Information related to the disbursement of the bond proceeds will be posted online in docket [GW17-002](#) – In the Matter of the Grain Buyer Bond of H & I Grain of Hetland, Inc.

Are all unpaid sales made to H & I Grain eligible for bond proceeds?

Not all unpaid sales made to H & I Grain are covered by the bond. Grain that is subject to the terms of a voluntary credit sale contract, such as price-later or a deferred payment contract, is not covered by the bond according to state law.

What is a VCS contract?

VCS stands for voluntary credit sale. A VCS contract is a tool grain producers may use to defer payment and/or delay pricing of delivered grain. Some popular types of VCS contracts include:

Delayed Price or Price-Later – This type of contract allows the producer to deliver grain to the grain buyer but delay setting a price on the grain until the market is more favorable. These contracts are often used at harvest time when there is typically a dip in grain prices. When using this contract, the producer passes title of the grain to the buyer, but the producer retains the ability to price the grain at a later date when the prices may be higher. Grain buyers usually charge a fee to the producer when this type of contract is used.

Deferred Payment – This contract allows the producer to set the price for the grain delivered but defer payment to a later date. When this contract is used, title to the grain passes to the buyer but payment is delayed. Grain buyers usually pay interest to the producer when this type of contract is used.

There are other types of less popular VCS contracts available. All VCS contracts have three things in common: (i) title to the grain passes to the buyer upon delivery, (ii) payment for the grain is delayed beyond 30 days, and (iii) the transaction is not protected by the South Dakota statutory bond requirements.

[ARSD 20:10:12:13](#) requires the following statement to be placed in red or bold type immediately above the customer signature line on a VCS contract. "This contract is not protected by South Dakota statutory bond coverages." During grain buyer inspections, PUC inspectors verify that each buyer's VCS contract complies with this rule.

Why is there no bond coverage for VCS transactions?

The purpose of the grain buyer bond is to protect the grain producer who sells grain on a cash basis. When a producer enters into a VCS contract he takes the transaction beyond that of a straight grain sale. Rather, the producer is voluntarily entering the realm of an unsecured creditor. When this decision is made, the producer exposes himself to greater risk for a longer period of time. The grain buyer bonds are not intended to protect this type of transaction. This is why [ARSD 20:10:12:13](#) requires notice of no bond coverage to be printed on all VCS contracts.

What recourse do producers that sold grain to H & I Grain on a VCS contract have?

The PUC recommends individual grain producers obtain legal counsel. As a licensing agency, the PUC's authority is provided by state law enacted by the South Dakota Legislature. Producers may have financial or other interests outside the PUC's jurisdiction and the commission urges producers to protect those interests.