
STAFF MEMORANDUM REGARDING ROSLYN ELEVATOR-UPDATE

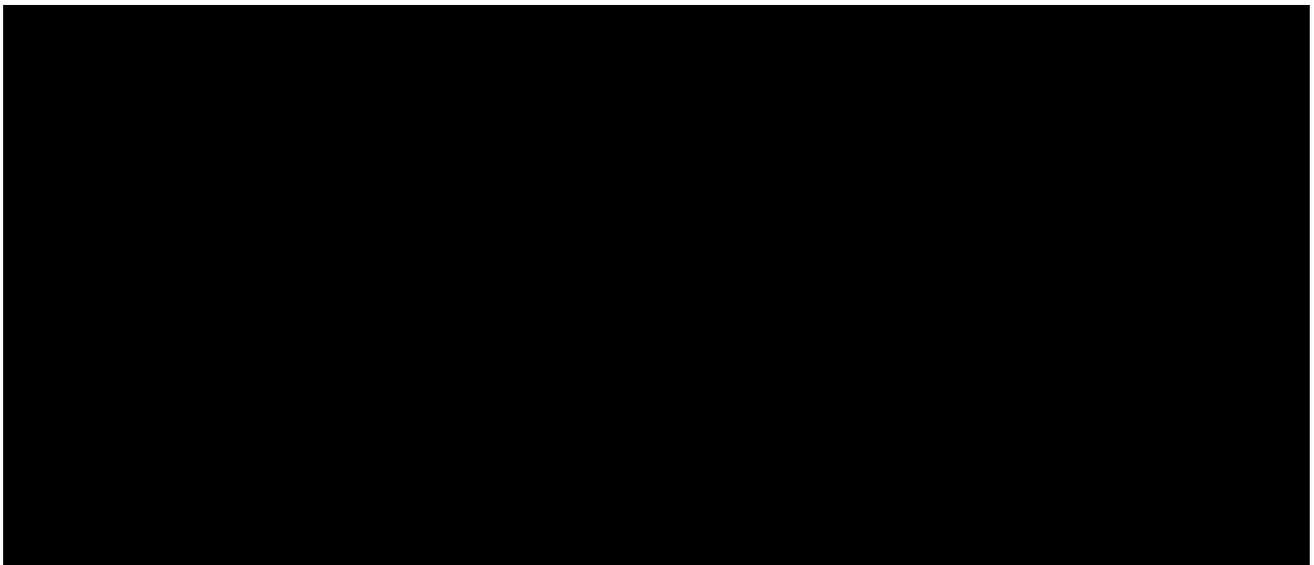
TO: COMMISSIONERS AND ADVISORS
FROM: GRAIN WAREHOUSE PROGRAM STAFF
RE: GW22-002, Roslyn Elevator, Roslyn, SD
DATE: June 7, 2022

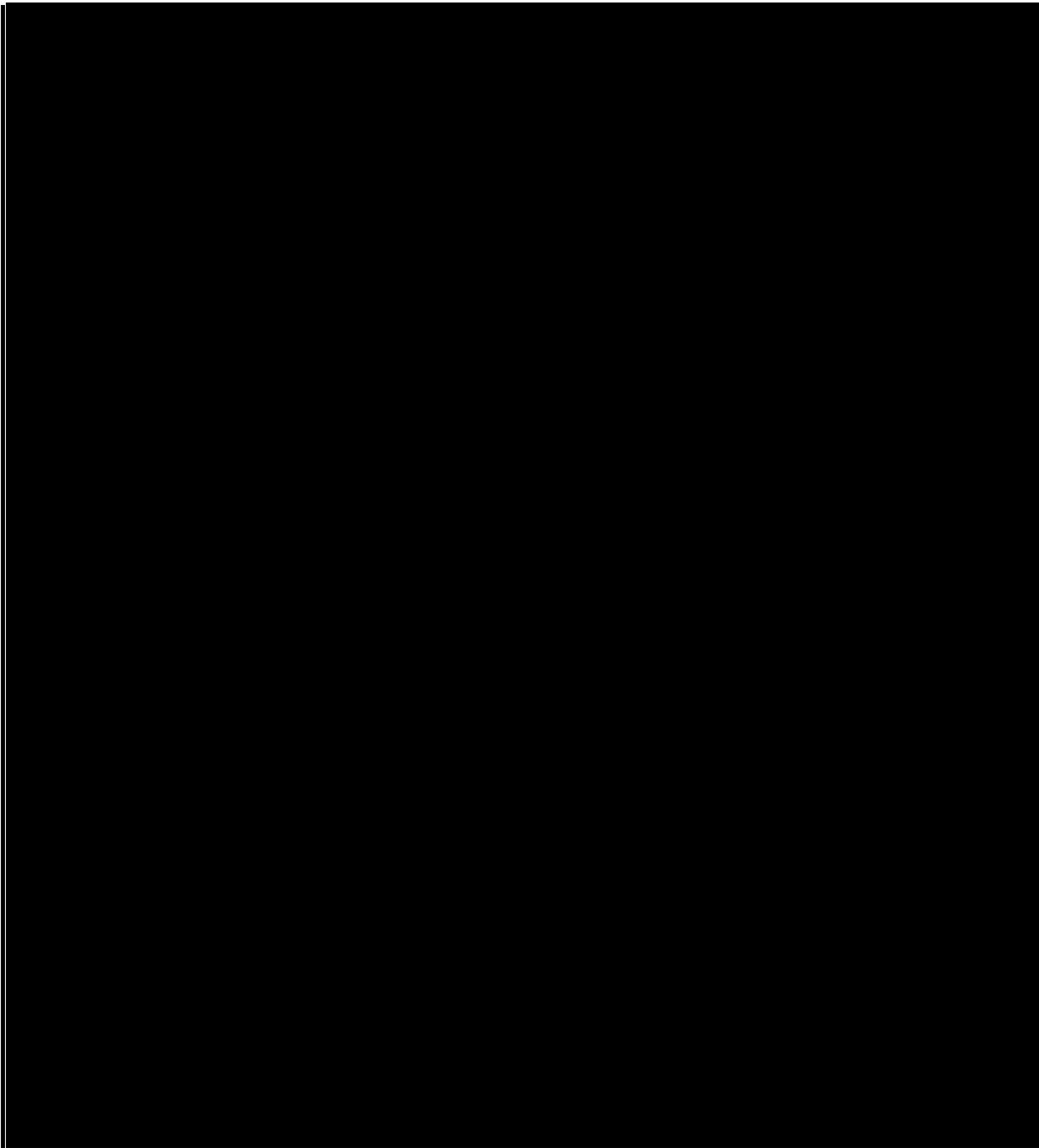
Commission Staff (Staff) submits this Memorandum to provide further explanation regarding the licensing and financial status of Roslyn Elevator, located in Roslyn, South Dakota.

Roslyn's Financial Status

Since Staff filed this docket on February 3, 2022, Staff has been in extremely close contact with Steve Schmidt and Roslyn Elevator (Roslyn). Staff has conducted twice weekly inspections of Roslyn and Mr. Schmidt has been in communication with Staff almost daily regarding operations and Roslyn's financial status. Roslyn has made considerable progress in improving its financial condition, significantly reducing much of the short-term debt by pricing out VCS contracts and thus adding the related storage and service fees to Roslyn's income and removing short term debt from Roslyn's balance sheet. Roslyn's specific financial information between February and the most recent draft May 23 balance sheet were filed as Confidential Exhibits on June 1, 2022, and the financials are further explained below.

****BEGIN CONFIDENTIAL****





****END CONFIDENTIAL****

Financial Review

While Roslyn's balance sheet is not fully in compliance with financial requirements, and while Staff is concerned about Roslyn's bank situation and with Roslyn incurring additional VCS contracts at this time, Staff also believes Roslyn is in a much better financial situation than in February. Roslyn's progress in clearing VCS contracts of Roslyn's financial statement has reduced Roslyn's short-term

liabilities and created a bit of revenue from storage. Additionally, Roslyn has continued to make payments on all loans, paying down the debt and showing Staff that the main issue with Roslyn's financial circumstances in the impending line of credit. Staff's assessment is that if the line of credit, or even a portion thereof were restructured into a long-term loan, Roslyn would be in full compliance with financial licensing requirements and would be able to continue making payments on such a loan. However, the ability to continue making loan payments may be significantly diminished if Roslyn were unable to continue operating as a grain buyer or warehouse.

License Status

Roslyn holds a Grain Warehouse license and a Class A Grain Buyer license (currently suspended) for licensing year 2021-2022. Roslyn has applied for a Grain Warehouse license and a Class A Grain Buyer license for licensing year 2022-2023. Roslyn has been able to secure a bond for licensing year 2022-2023. ARSD 20:10:11:15 requires a positive net worth and working capital (assets greater than current liabilities) for a Grain Warehouse license. ARSD 20:10:12:15 requires an applicant for a Class A grain buyer license show positive net worth of \$100,000 and positive working capital (assets greater than current liabilities) and for an applicant for a Class B grain buyer license show a positive net worth and positive working capital (assets greater than current liabilities).

While Roslyn has made significant progress in coming into compliance with state financial requirements, looking strictly at the balance sheets as provided, Roslyn does not show positive net worth nor positive working capital. Therefore, it is not fully in compliance with the financial criteria set in administrative rule. However, ARSD 20:10:11:18 provides that the Commission may grant a waiver of any rule in the chapter (grain warehouse) if it finds the waiver would not be detrimental to depositors and is in the public interest. Similarly, ARSD 20:10:12:17 provides for a Commission waiver of any rule in the chapter (grain buyer) if the Commission finds that the waiver would not be detrimental to a grain seller and is in the public interest. These rules allowing for waivers of financial licensing criteria do provide the Commission with some amount of flexibility to grant a license if doing so would be in the public interest and not detrimental.

Staff's Analysis

At this point, Staff does not see a need to move forward with revocation proceedings for the FY22 license the Commission suspended in February, though current license restrictions should remain in place. As indicated in February, Staff's overarching concern was the effects Roslyn's line of credit and VCS contracts had on equity and net worth on Roslyn's balance sheet as well as the looming end-date on Roslyn's line of credit. In Staff's opinion, these factors put Roslyn out of compliance with state financial requirements and into an insolvent financial situation. It was Staff's opinion that entering additional VCS contracts could put producers at risk and worsen Roslyn's financial situation and that a pause on Roslyn's license was necessary. While these factors are still present, Roslyn has taken significant steps to rectify its financial position. Additionally, Staff conducted a more thorough review of Roslyn that shows Roslyn's financial situation is not as black and white as the balance sheet shows. Roslyn's bank has not called the note due in-full and has allowed Roslyn to continue making payments on the note while

Roslyn pursues other financing options. Roslyn has also indicated a desire to continue operating and has submitted an application for a FY23 grain buyer license. With this movement, and with the end of the current licensing year coming June 30, 2022, when the current license will expire, Staff does not believe moving forward with revocation proceedings will serve the interest of producers or the public. Instead, Staff believes a broader conversation about whether Roslyn could be licensed for FY23 will be more of a benefit and will inform Roslyn, producers, and the bank about how to proceed.

Since February, the majority of producers with VCS contracts have actually priced grain, allowing grain to be moved and producers paid. There are a few remaining producers with VCS contracts, and those will need to be priced either before the license expires or the contracts will be automatically priced on June 30, 2022. SDCL 49-45-11 requires those producers be paid within ten days after the license expiration date, so for those priced June 30, 2022, payment is required under state law no later than July 11, 2022. The conditions of the suspension have allowed Roslyn to operate, with Staff approval, as necessary to clean up spoilt grain as well as clean up Roslyn's finances as possible. Staff does not believe further action on Roslyn's license will be beneficial for producers or Roslyn, so Staff recommends not proceeding with a revocation proceeding at this time, but instead leave the current suspension with conditions in place until the license expires on June 30, 2022, or a FY23 license is issued.

Staff Recommendation

As far as Roslyn's application for FY23 grain warehouse and grain buyer licenses the Commission could deny both a Grain Warehouse and Grain Buyer Licenses for failure to meet financial requirements or consider granting a waiver of the financial requirements to grant a grain warehouse and/or a Class A or Class B grain buyer license.

Staff recommends the Commission to waive the financial requirements in ARSD 20:10:11:15 and grant Roslyn a grain warehouse license for FY23. Through the years, Roslyn has been a solid company in good standing with the PUC. Although the straight balance sheets do not meet the minimum working capital and net worth requirements, Staff does not believe operation as a Grain Warehouse would be detrimental to depositors. Roslyn has obtained a grain warehouse bond in the amount of \$25,000 and provided that to Staff. This bond would cover unexpected losses. Additionally, depositors in a grain warehouse retain title to their grain so Staff has no concern with a loss to depositors and Roslyn does carry stock insurance. Allowing Roslyn to continue operating as a grain warehouse would be in the public interest. As mentioned in Staff's initial filings, Roslyn is the only elevator in the area, with the closest elevator 12 miles away. Completely removing Roslyn as an option for storage in the area could pose hardship on the producers in the area, especially with high fuel costs which could make transporting grain to another facility much more expensive. Roslyn does have storage facilities available, and it seems impracticable to prevent Roslyn from operating those facilities to warehouse grain as long as the facilities are in Roslyn's possession, especially with no recognizable detriment to depositors.

A Class B license does not raise the same concerns as a Class A license. Not only are transactions limited to \$5 million with a Class B license, VCS contracts are not permitted. Because of this, there would be bond coverage for transactions, providing an additional level of security for producers. However,

limiting Roslyn to \$5 million in purchases does not seem necessary in this case. With grain prices high, \$5 million in purchases is likely to be made very quickly and restrict Roslyn's ability to move grain, limiting Roslyn's ability to turn revenue. While believes a Class B license would be in the public interests and would not be detrimental to producers, Staff views a Class B license as an option if the Commission does not believe a Class A license appropriate.

As far as a grain buyer license for FY23, the banking situation is significant when contemplating whether a waiver is appropriate, especially where a Class A license is concerned. While Roslyn has not drawn on a bank note to operate for some time, it is concerning that Roslyn does not have an available line of credit and that the bank can come in at any time to seek to collect on the line of credit in full. It is also concerning that the bank, as a secured creditor would collect before any producer could collect. This is especially concerning because the bank could move to foreclose on the facility and potentially have significant control over the sale of the facility, potentially leaving producers unable to collect any amount owed. Because of this, Staff does have concern about Roslyn entering into additional VCS contracts before the bank situation is resolved. However, a Class A license would allow Roslyn to make grain purchases in excess of \$5 million, which aligns with Roslyn's historic volume of grain transactions. If the transactions under a Class A license were limited to cash only purchases until the bank situation is resolved, Roslyn's bond would provide protection to producers. With such a limitation, Staff believes it would be in the public interest to allow Roslyn to continue to operate as a grain buyer and doing so would not be detrimental to grain sellers. Staff supports granting a waiver of the financial requirements and granting a FY23 Class A grain buyer license to Roslyn.

Conclusion

At this point, unfortunately this situation is in a catch-22 scenario. Denying a Class A license to Roslyn will limit purchases to less than five million dollars. Allowing a Class A license also creates a problem by allowing current delayed price contracts to continue and not expire on June 30. The deferred contracts can remain on the books to be paid in 2023, 2024, and 2025 without any concerns from Staff.

Staff recommends granting the waiver of 20:10:12:15 for financial minimums for the Class A grain buyers license and the warehouse license. Staff also recommends granting a Class A license with the exception of VCS contracts. However, at this time, it is Staff's intent to request a deferral of this docket at the June 8 commission meeting. This will allow us to take back the feedback from the meeting. In addition, it is our understanding the Roslyn obtained legal counsel last week. A week's deferral will give Roslyn's counsel time to consider the discussion at the June 8 meeting and work with Staff to bring a recommendation based upon that feedback.