



National Grain and Feed Association Arbitration Decision

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July 12, 2001

Arbitration Case Numbers 1975 AND 1975-B Case Number 1975

Plaintiff: Farmer's Cooperative of Lidgerwood, Lidgerwood, N.D.

Defendant: Peavey Co., Omaha, Neb.

Case Number 1975-B

Plaintiff: Peavey Co., Omaha, Neb.

Defendant: Cargill Inc., Minneapolis, Minn.

Statement of the Case

On Jan. 28, 1998, Peavey Company ("Peavey") purchased a train of yellow corn from Farmer's Cooperative of Lidgerwood, N.D., ("Farmer's Co-op") for shipment in November 1998.

The transaction specified U.S. No. 2 yellow corn, and referenced a discount schedule that provided for certain discounts to be applied for delivery of lesser-quality corn. The contract stated clearly that "first official" grades would govern in the trade, a fact that was not disputed by any of the parties involved.

On Nov. 24, 1998, Farmer's Co-op tendered to Peavey a 54-car train of yellow corn. Origin samples were obtained and graded by the North Dakota Grain Inspection Service, a private inspection agency authorized by the U.S. Department of Agriculture's Grain Inspection, Packers and Stockyards Administration (GIPSA) to perform official inspection services. The grade determination of the corn contained in several of the cars was of a lower quality than what was allowed on the original discount schedule. Thus, the original discount schedule was modified by agreement of the parties. The train then was billed to Peavey at Kalama, Wash. The parties also did not dispute the aforementioned facts.

Later on the day of Nov. 24, 1998, Peavey sold the train to Cargill Inc. ("Cargill"). The origin grades were available at that time and the transaction was made on the basis of those inspection results. While Cargill's written contract was confusing with respect to the application of "first official" grades, Cargill subsequently agreed that

"first official" grades were to govern in the contract. The train then was reconsigned to Cargill and billed to its facility in Duluth, Minn. Transit time was four days.

During the process of unloading the train at Duluth, Cargill determined that some of the corn on the train had a sour odor. Cargill ceased unloading operations and obtained destination samples and grades from the State of Minnesota Grain Inspection Service, a state agency authorized by GIPSA to perform official inspections. The destination grades determined that 41 of the cars in the train were sour. Based upon the destination grades, Cargill rejected the train as "unmerchantable" pursuant to the terms outlined on the reverse side of its contract. Peavey, whose contracts also required delivery of "merchantable quality" product, responded by rejecting the train back to Farmer's Co-op and replacing it with another train to fulfill its contractual obligation to Cargill.

Subsequently, the rejected cars were disposed of by Farmer's Co-op at two different destinations. Official grades were obtained at each final billed destination. Those inspection results determined that 14 cars contained sour corn, compared to the 41 cars rejected at Duluth on those grounds.

Farmer's Co-op responded by submitting a claim against Peavey for losses totaling \$21,183.37, which consisted of additional inspection charges, discounts and freight incurred as a result of Peavey's alleged improper rejection of the shipment. Farmer's Co-op also sought interest on its claimed losses as of Dec. 10, 1999.

In its claim, Farmer's Co-op contended that contract terms specified that "first official" grades governed its contact with Peavey, and that, therefore, the rejection of the shipment on the basis of destination grades was invalid.

Peavey, contending that it was merely a "string" participant in this trade, requested that Cargill indemnify it for the losses claimed by Farmer's Co-op.

Cargill countered by contending that its contract with Peavey called for delivery of grain of "merchantable quality." To justify its position, Cargill cited the Uniform Commercial Code (UCC) definition of "merchantable goods," which reads as follows:

*"Goods to be merchantable must be at least such as pass (a) without objection in the trade under the contract description; and (b) in the case of fungible goods, are of fair average quality within the description, and are fit for the ordinary purposes for which such goods are used; and (c) run, within the variations permitted by the agreement of even kind, quality and quantity within each unit and among all units involved; and (d) are adequately contained, packaged, and labeled as the agreement may require; and (e) conform to the promise or affirmations of fact made on the container label if any."*¹

Cargill stated that because the affected cars did not comply with the standard for "merchantable quality" as defined in the UCC, it was justified in rejecting the shipment.

The Decision

While Cargill's position regarding "merchantable quality" was not completely without merit, the most pertinent fact in this case was that all parties agreed to settle the contracts in dispute on the basis of the results of "first official" grades. In this case, those were the official grades determined at origin by the North Dakota Grain Inspection Service.

If any of the parties had wished to question the integrity of those grade determinations, a process exists through which that could have been done. That process involves filing a federal appeal through GIPSA on the samples that were obtained at origin. Under the federal appeals process, the appeal results govern if they differ from the original inspection result. Therefore, since the grade determination at origin qualified as an official inspection (since the private inspection agency had been designated such authority by GIPSA), the arbitrators relied entirely upon the contracted terms, which very clearly stipulated that the trades be settled based upon "first official" grades. The samples and grades obtained at destination had no bearing on this matter and merited no consideration.

Therefore, the arbitration panel found unanimously in favor of Farmer's Co-op. Further, the arbitrators audited Farmer's Co-op's claims and found no fault in its request for compensation in the amount of \$21,183.37. In addition, the arbitrators awarded Farmer's Co-op interest on the claimed amount at the rate of 8 percent A.P.R. from Dec. 18, 1998 until March 31, 2001, which totaled \$3,872.20, pursuant to the NGFA Grain Trade Rules. NGFA Grain Trade Rule 15(D) states that destination weight certificates should be furnished to the seller or its designee by the unloading party within five business days of the unloading date. That would have required that Cargill furnish weight certificates and evidence of weighing charges to the seller(s) by Dec. 4, 1998. The arbitrators believed it was reasonable to expect that all parties should have been able to complete the invoicing and accounting work required to provide final settlement to Farmer's Co-op within two weeks of unload (by Dec. 18, 1998).

Since these damages were a direct result of Cargill's improper rejection of the shipment in question, the panel determined that Cargill alone was liable for the entire amount.

The Award

Therefore, it is ordered that Cargill make immediate payment in the amount of \$25,055.57 to Farmer's Cooperative Elevator of Lidgerwood, N.D.

Submitted with the unanimous consent and agreement of the arbitrators, whose names appear below:

Charles Elsea, Chairman
Senior Vice President
The Scouler Co.
Salina, Kan.

Warren Duffy
Vice President, Export Operations
ADM/GROWMARK River Systems Inc.
Ama, La.

Gil Peichel
Manager
F.C. Stone LLC
Dell Rapids, S.D.

¹ The NGFA's Trade Rules do not contain a specific definition for "merchantable quality."