



National Grain and Feed Association

Arbitration Decision

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March 13, 2008

Arbitration Case Number 2169

Plaintiff: ADM Grain Co., Overland Park, Kan.

Defendant: Heartland Co-op, West Des Moines, Iowa

Statement of the Case

This dispute involved a rail freight contract between the plaintiff, ADM Grain Co., and the defendant, Heartland Co-op, for the sale of 200 Union Pacific (UP) Railroad Guarantee Pool cars (100 cars for each half of the month of October 2006).

The cars were contracted through a freight broker, which was not a party in this case, under that broker's contract number 34048 dated Aug. 10, 2006. The pool car sublessor, Louis Dreyfus Corp. (LDC), Kansas City, Mo., previously had sold the cars to ADM. LDC was not a party to this dispute, but was involved in the string of underlying events resulting from the UP's response to actions taken by Heartland following the railroad's failure to deliver the cars within the order period.

One hundred cars were ordered into Heartland's Carlisle, Iowa, facility in accordance with the contract terms for the last half of October. UP then assigned a guaranteed pool number of 527114. Heartland paid ADM for the cars. Neither party disputed the terms of the contract, the contract price or whether payment for the cars was made.

The UP operates several grain car programs under its Grain Car Allocation System Rules (GCAS). These rules cover guaranteed pools and list a series of options available to pool car users if the railroad is late in delivering the cars. After the UP failed to deliver

the cars in October, they were rolled into the first half of November as a non-guaranteed order. After the UP failed to deliver the cars by Nov. 15, they were canceled by Heartland on Nov. 16, 2006. The dispute in this case centered on what happened following Heartland's decision to cancel the cars.

After the cancellation by Heartland, the UP penalized LDC, as the sublessor and ultimate holder of the cars, with the GCAS pool cancellation fee of \$250 per car for non-use of the cars. The UP subsequently decreased LDC's November 2006 pool payment by \$25,000 (\$250 x 100 cars). LDC then billed ADM for the cancellation fee of \$25,000, and ADM paid this amount to LDC. In turn, ADM billed Heartland for the same charge. Heartland refused payment, citing the UP's own GCAS cancellation rules.

The arbitrators determined that this case should be decided based upon the "custom of the trade" as it pertained to UP pool freight involved in this contract. In doing so, they interpreted and applied the contract terms pertinent to a situation in which placement of the cars was late. That, in turn, led to the pertinent question of whether a railroad, the UP in this case, may charge a penalty for its own failure to provide cars within the contracted delivery period, as well as the treatment of such non-performance within the context of the NGFA Trade Rules.

The Decision

The arbitrators concluded that there did not appear to be a well-defined custom of the trade applicable in this case within the context of the UP's GCAS rules, which were cited by both parties.

The arbitrators noted that Section 2 of the GCAS rules, which governs the UP's Guaranteed Freight Pool, provides that if the UP fails to spot cars in the specified period, shippers may cancel the order and claim a \$250 per car penalty from the railroad. The UP

requires that this claim form be submitted no later than 60 days after the specified period or a claim will be denied. The UP's rules also stipulate that orders not canceled are to be rolled to the next half-month period, and that all GCAS rules and guarantees continue to apply. Section 2 also states, "if Shipper fails to load the required number of cars during a given month, their following month's sublease rental payment will be reduced based on the terms of the sublease agreement." Section 2 further states, "If cars are not

placed during the current half or order is not canceled as described above, order will roll to the next period. All rules and guarantees apply as if the order were for the new period.”

The arbitrators also noted that Section 2 of the GCAS rules refer to Section 5 for “additional guarantee terms.” Section 5 provides for the validity of guarantees if the orders do not exceed existing track, line and service capacity at the origin facility. The arbitrators determined that the original last half October order in this case did not exceed the capacity at the origin facility. However, once the order was left unfilled in the last half of October, the order rolled to the first half of November. The UP, determining that Heartland’s Carlisle, Iowa, facility already had the threshold of four orders in place for the first half of November, exercised its option under Section 5 to remove the guarantee provisions from all orders in excess of those four.

The arbitrators further noted that Section 5 of UP’s GCAS rules specifies that when service levels are exceeded, it is the responsibility of the elevator to communicate with the pool or voucher owner. In this case, the arbitrators determined that the cars were sold by LDC to ADM, and then by ADM to Heartland, and they were paid for by each purchasing party. Through these transactions, LDC indirectly relinquished its controlling interest in the cars. Even though Heartland never received the cars, the arbitrators believed that out of professional courtesy, Heartland should have notified LDC and ADM of its intent to roll the want dates and not cancel them when the cars were late in October.

The arbitrators concluded that the UP GCAS rules clearly stated the options available for cars that carry a guarantee, but which still are not delivered by the last day of the guaranteed delivery period. However, the arbitrators also believed that the UP’s tariff was extremely vague, in that it did not directly address the options available when cars are late, roll to the next delivery period and lose their guarantee, and then still are not delivered – making them late again – all because of the carrier’s non-performance. The arbitrators observed that clarity in the UP GCAS tariff regarding options available for cars that have lost their guarantee status would have provided better guidance to both parties involved in this case, as well as to the industry in general.

ADM maintained that its interpretation of the custom of the trade meant that if the actions of a user of UP freight resulted in

penalties being assessed by the railroad, the party whose actions caused the penalty ultimately should be liable for any damages imposed. Meanwhile, Heartland contended that the cancellation options in the tariff regarding guaranteed pool cars that are not timely delivered applied to its cancellation of order number 527114 on Nov. 16, 2006 and as such, no penalties were due. The arbitrators again noted that UP’s GCAS rules cited specific timelines and deadlines for canceling late cars.

Heartland further contended that conversations occurred between it and the UP prior to Heartland’s cancellation. The arbitrators noted, however, that Heartland did not provide copies of facsimiles or other time-stamped records of such discussions or actions by Heartland in this case, which the arbitrators determined would have been useful.

Further, the arbitrators concluded that Heartland was in error for not contacting LDC when the cars were rolled because the cars’ status had changed from guaranteed to non-guaranteed based upon Heartland’s response to UP’s failure to deliver the cars during the original order window.

The arbitrators concluded that the cars were ordered and paid for in accordance with the contract terms. The issue then became whether it was a custom of the trade that a buyer of guaranteed freight should be held liable for the railroad’s non-performance and, further, that the buyer ultimately be held liable for charges assessed for a product that was never delivered. The arbitrators determined that the crux of this issue was that contracts defined under the NGFA Trade Rules carry the obligation to supply the product sold. Any party which provides a promise of a product has a contractual obligation to supply what was sold or promised. The arbitrators decided that the UP entered into a contract with LDC to provide cars and, therefore, was obligated to provide the cars. The UP subsequently defaulted on this obligation. Therefore, the arbitrators found that the UP was not within its rights to penalize LDC for its default on a contractual obligation.

The arbitrators ruled that the obligation to supply cars was never fulfilled and, as such, the buyer, Heartland Co-op, was within its rights to remedy the non-performance in a customarily acceptable manner. In this case, that remedy was cancellation of the cars without fear of penalty.

The Award

Therefore, the arbitrators ruled in favor of Heartland. The arbitrators also declined to award costs, interest or arbitration fees to either party.

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

Jerry Cope, Chair
Transportation Manager
South Dakota Wheat Growers Association
Aberdeen, S.D.

Tom Bright
Senior Merchandiser
Johnston Enterprises
Enid, Okla.

Kevin Thompson
Senior Manager
The Scoular Co.
Preston, Idaho