



National Grain and Feed Association

Arbitration Decision

1250 Eye St., N.W., Suite 1003, Washington, D.C. 20005-3922
Phone: (202) 289-0873, FAX: (202) 289-5388, E-Mail: ngfa@ngfa.org, Web Site: www.ngfa.org

January 29, 2009

Arbitration Case Number 2171

Plaintiff: Bartlett Grain Co. L.P., Kansas City, Mo.

Defendant: A&G Farms and Aaron Johansen, Robinson, Kan.

Statement of the Case

This case concerned alleged corn contracts entered into between February 2006 and January 2007 between Bartlett Grain Co. L.P. (Bartlett), the buyer, and Aaron Johansen (Johansen) and A&G Farms, the sellers.

Johansen and his relation, Greg Bachman (Bachman), grew corn in northeast Kansas. Johansen sold grain under his own name. Bachman sold grain under the name of GB Farms. Bachman and Johansen also said they had plans to farm some ground together, and sold grain jointly under the name of A&G Farms. While the three entities appear to all be separate, it was not uncommon for Johansen to sell grain to Bartlett under any or all of the three names. On one occasion, a market adviser also sold grain for A&G Farms.

The actions that triggered this dispute began on April 13, 2007, when Bartlett personnel said they began hearing stories that Bachman was contemplating bankruptcy. On this date, according to information provided by Bartlett, the following positions were in place:

Johansen:

- ▶ There was \$115,537.91 due to Johansen on grain already delivered.
- ▶ There were 941.07 bushels of old-crop contract corn yet to be delivered.
- ▶ There were 200,000 bushels of new-crop contracts to be delivered from the 2007 crop.

GB Farms:

- ▶ There was \$15,292.16 due to GB Farms on grain already delivered.
- ▶ There were 10,208.94 bushels of old-crop corn yet to be delivered.
- ▶ There were 200,000 bushels of new-crop contracts to be delivered from the 2007 crop.

A&G Farms:

- ▶ There were 150,000 bushels of new-crop contracts to be delivered from the 2007 crop.

After hearing the stories about Bachman considering bankruptcy, Bartlett immediately reacted by putting a hold on all grain payables in its possession involving GB Farms and Johansen. In Bartlett's words:

"If the parties were willing and able to honor their contracts, Bartlett wanted to buy the corn. If the parties were not willing or able to honor their contracts, Bartlett needed to know, so that it could eliminate market risk in a time of generally rising commodity prices. For that reason, Bartlett needed assurance that Bachman, Johansen and A&G Farms would perform on their contracts. On April 25, Bartlett made its formal demand for 'adequate assurances' of GB Farms and to Johansen and A&G Farms."

The demand came in the form of letters from Bartlett requiring GB Farms, Johansen and A&G Farms to meet a margin call on the open contracts. Bartlett demanded that the other parties post margin by the close of business on April 27, 2007.

Several email exchanges of information subsequently occurred between the attorney representing Bartlett and the attorney representing GB Farms, Johansen, and A&G Farms. The arbitrators could list pages of information gathered from this exchange of information. However, the arbitrators have elected to minimize the details and set out only the information of most value in determining their final opinion on the case.

First, in reaching a decision, the arbitrators noted that there were two different forms of contracts used by Bartlett in the contracts with

Johansen and A&G Farms. One form was used until November 2006. A different contract form was used after that date. After switching to the new contract form, Bartlett attempted to amend the originals by later sending out a second notice with the new language on the back. Since both parties referred to paragraph 10, found only on the new contract form, and both argued an interpretation of paragraph 10, the arbitrators deduced that both parties accepted the new contract form as being in place. Therefore, the arbitrators used the new contract language in determining the outcome of this arbitration case.

Paragraph 10 of the contract stated:

“Adequate Assurances. When buyer has reasonable grounds for insecurity with respect to Seller’s performance, Buyer may demand adequate assurance of Seller’s performance. Buyer may demand pay-

ment from Seller up to an amount equal to the difference between the Contract price and the then prevailing market price for the commodity. Seller shall provide such adequate assurance within 48 hours of the receipt of such a demand. Seller’s failure to provide adequate assurance shall constitute Seller’s repudiation of this Contract. In the case of repudiation, Buyer has the right to pursue all legally available remedies, including but not limited to recovery of its losses, damages and costs, including a reasonable attorney’s fee.”

At the close of business on Friday, April 27, 2007, when Bartlett determined that, in its opinion, it had not received adequate assurance from Johansen or A&G Farms, Bartlett decided to effectively close out all outstanding contracts. This action was taken on Monday, April 30, 2007.

The Decision

Cutting through the volumes of information pertaining to this arbitration case, in the opinion of the arbitrators, the case came down to determining: 1) whether Bartlett had reasonable grounds for insecurity so as to justify demanding adequate assurance; and 2) whether Johansen had failed to provide adequate assurance so as to justify Bartlett closing out the accounts and contracts of Johansen and A&G Farms. If Bartlett was justified in demanding adequate assurance, then Bartlett was entitled to an award for its loss. If Bartlett did not have adequate grounds for closing out the contracts, then Johansen and A&G Farms would be entitled to recover. Thus, the questions to be answered were:

- ▶ Did Bartlett have reasonable grounds for insecurity?
- ▶ Did Bartlett allow Johansen and A&G Farms enough time to supply information, and was the information supplied by these parties sufficient to address Bartlett’s concern that grain would be delivered against the contracts?

In the exchange of information in April 2007 between attorneys representing Bartlett and Bachman, GB Farms, Johansen and A&G Farms, it became common knowledge that indeed, Bachman and GB Farms were filing for bankruptcy protection. As a result, Bachman and GB Farms were removed from this arbitration case. Bartlett acknowledged this in its rebuttal argument, stating, “As indicated in the revised arbitration services contract, the only parties to this dispute are Bartlett, A&G Farms and Aaron Johansen.” Therefore, the arbitrators made no decision pertaining to any of the GB Farms contracts.

Next, the arbitrators considered the position of A&G Farms. A&G Farms LLC was set up as a limited liability company with the intention that Johansen and Bachman would both have ownership interests. After Bachman filed for bankruptcy,

Johansen became the sole owner of the LLC. Although the State of Missouri does not have any record of A&G Farms LLC or its right to do business in the State of Missouri, A&G Farms LLC is a legally filed LLC in the State of Kansas, and does officially exist. As a result, the A&G contracts were considered by the arbitrators.

The remaining contracts of Johansen were considered in this arbitration case as well.

As stated previously, the main question to be answered in this arbitration case was, “Did Bartlett have reasonable grounds for insecurity to demand adequate assurance and were Johansen’s responses a basis for Bartlett to close out the contracts?”

On pages 3, 4, 5, and 6 of Bartlett’s rebuttal argument, Bartlett listed five reasons for its concerns with Johansen and A&G Farms:

- ▶ Johansen suddenly stopped delivering 2006 corn to Bartlett.
- ▶ Rumors arose that Johansen’s uncle/business partner was declaring bankruptcy.
- ▶ Input providers advised Bartlett that Johansen had not paid on invoices for his fertilizer and would be unable to purchase seed.
- ▶ Creditors began to call about Johansen’s threatened bankruptcy.
- ▶ The price of corn was rising.

The arbitrators addressed each of these five reasons individually.

▶ **Johansen Suddenly Stopped Delivering 2006-Crop Corn to Bartlett:** On page 3 of its original argument, Bartlett stated that, “In January and February 2007, Johansen delivered HYC and WC to Bartlett facilities. Deliveries stopped abruptly in early March. [A representative of Bartlett] called Johansen throughout March and April, urging him to deliver his corn.” This statement clearly showed concern. However, Bartlett’s concern was inconsistent. Under Tab 11 of Bartlett’s own original argument, a letter dated April 25, 2007 from Bartlett to Johansen stated: “You have delivered substantially all of your 2006 white and yellow corn obligations....You have advised us that a broken bin sweep has prevented you from delivering the last 941.7 bushels of your 2006 yellow corn obligations. We have told you that we would accept the corn when you got the equipment repaired.”

Although the arbitrators did not have access to the conversations that must have taken place some time in early April, the statements written on April 25 by Bartlett made it clear that Bartlett had accepted the reasons given by Johansen for the abrupt halt in deliveries, and that Bartlett agreed to accept delivery at a later time. Based upon this conclusion, this asserted concern was not acceptable grounds for reasonable insecurity.

▶ **Rumors Arose that Johansen’s Uncle/Business Partner Was Declaring Bankruptcy:** Under Tab 13 of Bartlett’s original argument, Bachman confirmed the rumors about GB Farms’ financial problems and informed Bartlett that GB would not be delivering on its contracts. Bartlett argued that A&G Farms was a partnership between Johansen and Bachman, and not a separate legal entity (i.e. a duly formed limited liability company). Under this assumption, Bachman’s financial problems and bankruptcy would have threatened the financial viability of the partnership. Of the two contracts with A&G Farms, one was signed on behalf of “A&G Farms LLC” and one simply as “A&G Farms.” As stated above, the evidence showed that “A&G Farms, LLC” was formed by the filing of Articles of Organization with the Kansas Secretary of State on Nov. 30, 2006. Johansen subsequently became the sole owner of the limited liability company. Johansen’s attorney communicated these facts to Bartlett’s attorney on April 26, 2007. Therefore, the arbitrators determined that this asserted concern was not acceptable grounds for reasonable insecurity.

▶ **Input Providers Advised Bartlett that Johansen Had Not Paid on Invoices for Fertilizer and Would be Unable to Purchase Seed:** According to Bartlett, it received information that Johansen still owed a large sum of money on last year’s fertilizer bills, and would be unable to purchase seed for this year. Further examination of the details showed that Bartlett’s elevator facility manager had formerly worked for another company (hereinafter referred to as “Company A”). In an internal e-mail, Bartlett’s fertilizer/chemical manager said:

“[The elevator facility manager] from Waverly called today and said [Company A] had called him to talk about Johansen’s past due account. [The elevator facility manager] said he had sold him fert and white corn seed. [Company A] had applied the fert in the fall, which Johansen is past due on payment. As a result of his past due fert bill [Company A] has refused to deliver the white corn seed. With seed being in short supply it will be difficult to replace it with any other brand. It might be impossible to fulfill his contracts to us for next year. [The elevator facility manager] also said he had heard the he had filed bankruptcy.”

On April 26, 2007, through his attorney, Johansen responded, stating that he did not owe any fertilizer company for crops grown last year. He said he owed Company A for fertilizer applied to cropland the previous fall and invoiced earlier in 2007. Johansen stated that he intended to secure a note the following week to pay Company A for this fertilizer. He also stated that he had a note with another company for white corn seed sufficient to fulfill the seed needs of Johansen and A&G Farms, and that the seed was being stored in Hiawatha, Kan. Finally, he stated that he could produce a copy of the note for verification upon request.

At no time did Bartlett ask for verification to see if Johansen had indeed purchased the seed. At no time did Bartlett follow up with Company A to see if Johansen’s fertilizer bill was from the last year or the current year. At no time did Bartlett take any action to confirm that its concerns about Johansen’s ability to perform his duties on the outstanding contracts were valid. Instead, based upon the evidence submitted, Bartlett simply received some information from a former employer of one of its facility managers and decided that no further verification on its part was necessary.

The arbitrators concluded that Johansen made a good-faith effort to supply truthful information to Bartlett to ease its concerns. In the end, 100 percent of the information supplied by Johansen was correct. He did secure a note and paid off the fertilizer bill. He was able to take delivery on white corn seed from another company. Johansen took all action necessary to assure Bartlett that he had the financial wherewithal and the seed availability to perform his duties as required under the contract. Further, if Bartlett still had concerns after receiving this information from Johansen, Bartlett had an obligation to do further research. Instead, Bartlett disregarded the information provided by Johansen, and proceeded to close out all of his contracts anyway.

Based upon all the information provided, the arbitrators determined that Bartlett’s statements about unpaid fertil-

izer bills and Johansen's inability to secure white seed corn was not acceptable as a reason for requiring adequate assurance.

► **Creditors Began to Call about Johansen's Threatened Bankruptcy:** In an internal e-mail (Bartlett Tab 18), Bartlett's fertilizer/chemical manager said, "[the elevator facility manager] also said he had heard the he had filed bankruptcy." In another internal e-mail approximately 31 minutes later (Bartlett Tab 18), Bartlett's white corn merchandiser stated, "[Company A] said that Aaron [Johansen] threatened them w/ bankruptcy, but has not filed yet."

Nowhere else was there any reference to creditors calling about Johansen threatening bankruptcy. The arbitrators noted that the elevator facility manager was the one who actually talked with Company A. However, it was Bartlett's fertilizer/chemical manager and Bartlett's white corn merchandiser who talked about Johansen's threatened bankruptcy. In the only documentation supplied by the elevator facility manager, (Statement of [the elevator facility manager], written on Nov. 28, 2007), he never said anything about Johansen threatening bankruptcy. Instead, it appeared that decisions were made by Bartlett based upon rumor, with no research or effort to confirm. Therefore, the arbitrators determined that "Johansen's threatened bankruptcy" was not a reason for requiring adequate assurance.

► **The Price of Corn was Rising:** The arbitrators decided that the rising price of corn was a timing issue, not reasonable grounds for insecurity or an adequate assurance issue. If a party has a legal right to price out another's contracts, the fact that the price is increasing will make him want to do it sooner, rather than later. However, the price of corn has nothing to do with the necessity of adequate assurance that someone will deliver. If the rising corn price was a sufficient reason to make margin calls on Johansen, then it would have been reason enough for Bartlett to make margin calls on everyone with which it had open contracts. Bartlett apparently did not do that. Therefore, the fact that the price of corn may have been rising was not enough to justify Bartlett's actions.

Bartlett sent a letter to Johansen and A&G Farms asking for margin calls on all of their open contracts. The contract language in place allowed Johansen and A&G Farms up to 48 hours to make adequate assurance. Within 24 hours, Johansen and A&G Farms had responded to Bartlett's letter, answering each question in detail. It was evident that Bartlett believed that the only solution was for Johansen and A&G Farms to make the requested margin calls. The fact that Johansen and A&G Farms responded to each of Bartlett's areas of concern was not enough. It appeared that Bartlett already had determined that the only solution was margin calls. Thus, while Johansen and A&G Farms did not give the adequate assurance that Bartlett

expected, causing Bartlett to close out the contracts, the arbitrators concluded that the grounds for reasonable insecurity cited by Bartlett, especially when considered in light of the responses given by Johansen and A&G Farms, did not justify Bartlett's action.

Thus, the arbitrators determined that none of the five reasons stated by Bartlett provided sound reasoning for needing further adequate assurance nor justification for closing out the contract positions. Since Bartlett closed out all contracts when it did not have adequate reason to do so, the arbitrators ruled in favor of Johansen and A&G Farms. Bartlett was denied any and all of its requested relief.

Johansen requested the following damages (on behalf of Johansen):

- 1) Balance of payment due on contracts fulfilled for 2006 crops/grain. (*Of the \$115,537.91 owed to Johansen for grain previously delivered, Bartlett paid off a CCC loan for Johansen in the amount of \$100,268.54. Therefore the requested amount of payment was \$15,269.37.*)
- 2) Interest on payments withheld from contracts fulfilled for 2006 crops/grain. The principle amounts were not in dispute. The interest was calculated at 8.25 percent per annum, and pro-rated over a 365-day calendar year.
 - (a) Interest on total amount originally withheld of \$115,537.91 between the date of last delivery made and the date the partial payment of \$100,268.54 was sent to Commodity Credit Corporation on May 14, 2007.
 - (b) Interest on unpaid balance of \$15,269.37, covering the period between the date partial payment was sent to CCC on May 14, 2007 and Nov. 8, 2007.
 - (c) Additional interest from Nov. 8, 2007 and the date of award by the Arbitration Committee.

Johansen requested the following damages (on behalf of A&G Farms):

- 1) The market value at the time of breach was established using the value listed by Bartlett as the settlement price of their argument for white corn at \$3.695 bushel. The contract unit price was \$4.50/bushel. Therefore, the damages resulting from the wrongful termination of the A&G Farms contracts for the white corn was 50,000 bushels X (\$4.50 - \$3.695) = \$40,250.
- 2) The damages for the market value at the time of breach for the yellow corn to be delivered from the 2008 crops was taken at the value established by Bartlett in its argument at \$2,750.

It was also requested on behalf of Johansen and A&G Farms that they be reimbursed for reasonable attorney's fees and cost of arbitration.

The Award

It was the unanimous decision of the arbitrators that Johansen should receive, and therefore was awarded, any unpaid value for grain already delivered and held by Bartlett. This amounted to \$15,269.37. And while Johansen and A&G Farms had a legitimate reason for requesting the difference in the market value on the day Bartlett cancelled the contracts and the contract value, Johansen failed to mention the value he had already gained from the market after Bartlett cancelled the contracts. While Johansen requested \$43,000 in settlement for canceling his contracts, in reality, the market paid Johansen several times over that amount. It could not have been known at the time, but in the end, the greatest award Johansen could possibly have received was for Bartlett to cancel its lower-priced contracts. Johansen was denied the requested award of market value between the contract value and the value on the date the contracts were cancelled.

Likewise, the arbitrators denied interest, legal fees and arbitration costs. Thus, the final settlement due Johansen from Bartlett was \$15,269.37.

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

Tom Bressner, *Chair*
General Manager
Assumption Cooperative Grain Co.
Assumption, Ill.

Ron Barkema
Grain Department Manager
Prairie Land Cooperative
Hubbard, Iowa

Neil Grealy
Chief Legal Officer
Louis Dreyfus Commodities
Wilton, Conn.