



April 17, 2015

CASE NUMBER 2676

PLAINTIFF: INTERSTATE COMMODITIES INC., TROY, NY

DEFENDANT: NORTHWOOD EQUITY ELEVATOR COMPANY, NORTHWOOD, ND

STATEMENT OF THE CASE

This arbitration case developed between two firms that contracted in July 2012 for shipments of corn by rail in the fall of 2012 to several destinations in the southern and western U.S. The seller, Northwood Equity Elevator Co. (Northwood), and the buyer, Interstate Commodities, Inc. (Interstate), agreed in July 2012 to one allotment of 55,000 bushels (or 15 railcars) of U.S. No. 2 yellow corn for shipment in October 2012, and a second identical allotment for shipment in November 2012.

Twenty-one rail cars were loaded and graded U.S. No. 1, 2, 3 and 4 yellow corn by the U.S. Department of Agriculture Federal Grain Inspection Service (FGIS). FGIS noted on each certificate “*Seals Applied*” and “*Stowage area not examined. Top 10 feet sampled. Bottom not sampled.*” FGIS’s inspection did not indicate any concerns with the integrity of the hatches or rail cars.

The rail cars were billed out on or about Oct. 5, 2012. The cars then arrived at four destinations in four different states – Missouri, Oklahoma, Texas, and California – beginning about Oct. 22. The issues presented in this case began when concerns pertaining to the quality of the car loads (i.e., mold and must) surfaced on Oct. 23, and rejections of those loads by the end users followed the next several days. From Oct. 23 to Oct. 29, according to Interstate, 17 of the 21 rail car loads presented quality issues. The parties and end users successfully resolved issues concerning two of the rail cars, which are consequently not a part of this arbitration case. The other 15 of the rail cars in question were rejected in total by the end users.

THE DECISION

The arbitrators closely considered the arguments and facts presented by the parties in this case. In their analysis of this case, the arbitrators focused and relied heavily upon the overwhelming extent of the poor quality product that was sold by Northwood. It was compelling to the arbitrators that over three-fourths of the shipments arrived in such poor condition at different destinations in a short time frame.

The arbitrators reviewed the terms and conditions in the contracts that governed the transactions between the parties. The broker had issued contracts numbered 11331 and 11332 on July 16, 2012, which provided for the two shipments of 55,000 bushels of corn in October and November of 2012. The contracts also provided the following terms: “*Quality: Basis U.S. #2 Yellow Corn O/B: Basis 15.0% Moisture.*” The contracts further provided for “*Grades: Origin Official,*” “*Weights: Destination,*” and

“Discount Scale: Destination.” Although no signatures appeared on the copies of either contract submitted in this case, the arbitrators concluded that based upon the parties’ submissions each party had accepted these contracts.

The arbitrators also reviewed Interstate’s *“Confirmation of Basis Sale”* contract number P079843, also dated July 16, 2012, which correspondingly provided for the shipment of two allotments of a total of 110,000 bushels of U.S. No. 2 yellow corn between the parties. Contract P079843 further provided for *“1st official origin grades to apply”* and *“1st official origin weights to apply.”* The contract also stated in paragraph 5: *“Seller expressly represents and warrants that the commodity or commodities hereby purchased are of the grade indicated, and if none is indicated, that the commodity or commodities are suitable for feeding to poultry and livestock.”* Under the terms of paragraph 5, Northwood was contractually bound to deliver U.S. No. 1, 2, 3 and 4 grades of yellow corn, and to essentially track the grades on the origin certificates. Since the 15 rail cars in dispute were rejected by each of the four end users because the corn was in such poor condition and unfit for use as feed, the arbitrators determined that Northwood did not meet the terms of paragraph 5. The arbitrators also concluded that paragraph 7 of contract P079843 allowed for damages for a party’s failure to perform under the contract. Paragraph 7 stated as follows:

In the event Seller breaches this Contract in any manner, Seller shall be liable to Buyer for any and all damages, including consequential damages, incidental damages, and any lost profits incurred as a result thereof and shall pay Buyer’s reasonable attorney fees, court costs and expenses incurred in the enforcement of this contract and any collection activities related thereto. In no event shall Interstate Commodities, Inc. be liable for any special or consequential damages suffered by its principal in the contract.

The arbitrators concluded that with reference to either the broker contracts 11331 and 11332 or the Interstate contract P079843, Northwood failed to meet its obligations given how poor was the condition of the corn it sold that over three-fourths of the product was rejected at different destinations within a short time frame.

The arbitrators noted that when first notified by Interstate of the concerns related to quality of the shipped rail cars, Northwood’s response was by email on Oct. 24, 2012, to request Interstate’s assistance in mitigating damages at the least cost to Northwood. Specifically, the Oct. 24 email from Northwood’s location manager stated: *“Would Interstate please do the best to get our rejected corn cars unloaded at the least cost to Northwood Equity Elevator.”* The arbitrators determined that this response by Northwood was clear and unconditional.

Interstate then handled the role of re-grading, re-routing and re-selling the car loads at discounts into markets, which would accept the distinctly lower quality corn. After the initially rejected corn was shipped to new end users, Interstate invoiced Northwood for the related costs on Jan. 1, 2013, for a total of \$109,182.32. It apparently was not until this point that Northwood denied responsibility for those costs.

The question was presented in the case whether the sender of the Oct. 24 email, which triggered Interstate’s measures to remediate the damages in this dispute, was “authorized” to make any commitment on Interstate’s behalf. The arbitrators noted that writer of that email was identified in the communications between the parties as *“Manager Northwood Equity Elevator”* and had been the key person involved on Northwood’s behalf throughout the dealings with Interstate and this arbitration case. Therefore, the arbitrators concluded that he had authority upon which it was reasonable for Interstate to

proceed as it did. The arbitrators further rejected as insubstantial the claims that the elevator manager had been inappropriately enticed or coerced to make that statement.

Northwood also challenged specific components of Interstate's invoices. The arbitrators reviewed them closely. The invoices submitted in this case itemized the costs incurred by Interstate to remove the rejected rail cars from the original destinations and relocate them to new buyers with the discounts, freight, and demurrage charges listed for the shipments to each of the four destinations. The invoices did not appear to include any administrative, clerical, or similar expenses incurred by Interstate in providing this service nor did Interstate otherwise attempt to pass such costs on to Northwood. The arbitrators determined that the amounts claimed by Interstate were documented and appropriate.

The arbitrators considered how decisions in other arbitration cases may have allowed "first official grades, origin" to stand when the contract was silent on arrival condition, and the drop in quality condition of the commodity was slight to moderate. However, the arbitrators concluded that in this case – the compelling decline in quality in at least 17 of the 21 railcars (of which 15 cars were rejected in full) – removed any doubt whether the origin grades survived and the product was suitable under the contracts. The contracts and circumstances presented in those other cases were all vastly different.

The arbitrators also considered questions regarding the grading procedures employed and FGIS's inspection. Northwood argued that because it sold the grain "1st official origin grades to apply," it was not responsible for deterioration in the cars subsequent to the inspection certificate date. However, in rejecting this argument, the arbitrators again referred to limitations of the inspection indicated on the FGIS certificates, the buyer's right to inspect and reject shipments, and, again, the extent of the poor condition of the shipments.

THE AWARD

The arbitrators consequently decided that Northwood was liable for damages in the amount of \$109,182.32 owed to Interstate for its actual costs for remediation and final disposition of the 15 rejected rail cars. Any legal or arbitration fees were deemed to be each party's responsibility.

Decided: June 2, 2014

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

David Reiff, *Chair*
President
Reiff Grain & Feed Inc.
Fairfield, IA

James Dell
General Manager
Interstate Mills LLC
Owatonna, MN

Scott Lovin
Vice President
Ag Partners LLC
Albert City, IA



National Grain and Feed Association Arbitration Decision

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April 17, 2014

APPEAL CASE NUMBER 2676

APPELLANT/DEFENDANT: NORTHWOOD EQUITY ELEVATOR, NORTHWOOD, ND

APPELLEE/PLAINTIFF: INTERSTATE COMMODITIES, INC., TROY, NY

DECISION OF THE APPEALS COMMITTEE

This case was originally decided in favor of the plaintiff, Interstate Commodities, Inc. (Interstate). The defendant, Northwood Equity (Northwood), subsequently appealed the decision.

The Arbitration Appeals Committee individually and collectively reviewed all the arguments and supporting exhibits in the original case file of NGFA Arbitration Case No. 2676, along with the Statement of the Case, Decision, and Award issued by the original Arbitration Committee. The Appeals Committee also reviewed the Notice of Appeal filed by Northwood and the Reply to that notice filed by Interstate, as well as the appeal brief filed by Northwood. Interstate did not file an appeal brief.

The essential components of the case are as follows:

Northwood sold corn to Interstate through a broker. The broker issued two confirmation contracts to cover the trade. The terms (relevant to this dispute) in both confirmations are identical. Those applicable terms are as follows:

*FOB: Northwood, ND
Buyer's Cars*

Grades: Origin Official

The railcars were loaded by Northwood; officially graded at origin, accepted, and applied to the contracts; and billed by Interstate to various end users. Upon arrival, quality deterioration from the origin grades was noticed by the end users at destination and the cars were rejected.

The rejected cars were then resold and sent to other destinations by Interstate at a presented cost of \$109,182.32. Interstate is seeking reimbursement from Northwood for these costs.

Interstate claimed that Northwood was ultimately responsible for the costs of the rejected cars. In its submissions, Interstate argued that the applicable "industry standards" are that grain must be "cool and sweet and in good condition upon arrival at destination." The Arbitration Appeals Committee determined, however, that its duty was to, first, interpret the contract; second, apply the NGFA Trade Rules; and third, apply trade custom if appropriate. Therefore, the contract language and NGFA Trade Rules prevail over trade custom in this case.

The Arbitration Appeals Committee determined that three of the NGFA's Trade Rules particularly cover the essential issues of this case. The first applicable rule regards interpretation of the contract language.

Rule 3. Confirmation of Contracts

(C) When a trade is made through a broker, it shall be the duty of the broker to send a written confirmation not later than the close of the business day following the date of trade to each of the principals setting forth the specifications of the trade. Upon receipt of said confirmation, the parties shall carefully check all specifications therein, and upon finding any differences, shall immediately give notice to the other party to the contract and to the broker. If either party fails to give such notice, the terms and specifications contained in the confirmation issued by the broker shall govern the contract.

The Arbitration Appeals Committee consequently recognized the broker's confirmation contracts as the controlling contracts in this dispute.

The second rule upon which the Arbitration Appeals Committee relied was NGFA Grain Trade Rule 13.

Rule 13. Condition Guaranteed on Arrival of Rail Cars

(A) If grain is sold with condition guaranteed on arrival at destination, and the destination is provided in the billing instructions, the Buyer shall ascertain the condition and official grade of the grain. The Buyer shall report the condition and official grade to the shipper by a telephone call placed not later than 12 noon of the next business day after arrival of the car of grain at the destination.

If the Buyer fails to ascertain and report the condition and official grade as provided above, he shall waive all rights under the guarantee for that portion of the contract. Diversion of the shipment by the Buyer to a point beyond the original destination shall constitute an acceptance of the grain and a waiver of the guarantee.

NGFA Grain Trade Rule 13(A) applies only "If grain is sold with condition guaranteed on arrival." This clearly was not the circumstance in this case. The broker's confirmations formed the binding terms of the contracts. It was noted that the broker's confirmations are silent regarding any condition on arrival guarantees (such as cool and sweet).

Without a "condition guaranteed on arrival" clause in the contract the Arbitration Appeals Committee then referred to Grain Trade Rule 6 to determine which party bears responsibility for the grain condition loss during transit.

Rule 6. Passing of Title as Well as Risk of Loss and/or Damage

Title, as well as risk of loss and/or damage, passes to the Buyer as follows:

(A) On f.o.b. origin or f.o.b. basing point contracts, at the time and place of shipment. The time of shipment is the moment that the carrier accepts the appropriate shipping document.

The contracts in this case specified "FOB, Northwood, ND" – a f.o.b. origin trade. The risk of loss and/or damage transferred when the cars were billed. Thus, the risk of loss on the quality deterioration in this case was for the account of Interstate.

Interstate also argued that Northwood had accepted liability for the loss. In this regard, Interstate relied upon an email from Northwood asking Interstate to "do the best to get our rejected corn cars unloaded at the least cost to Northwood." The Arbitration Appeals Committee determined, however, that a simple request to assist with mitigation alone was not enough to transfer the liability in question.

AWARD

The original Arbitration Committee's decision relied heavily on the overwhelming extent of off- grades at destination. While understanding that a high percentage of cars were rejected at the various destinations, the Arbitration Appeals Committee focused upon the fact that "*Origin Official*" grades were specified in the contracts and that is what Northwood provided in fulfillment of its obligations. The Arbitration Appeals Committee noted that quality loss in transit is a common occurrence. The extent and degree of the quality is not the determining factor.

Therefore, the Arbitration Appeals Committee reversed the decision of the original Arbitration Committee and determined that no award be ordered in this case.

Decided: March 25, 2015

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

Roger Krueger, *Chair*
Senior Vice President, Grain
South Dakota Wheat Growers
Association
Aberdeen, SD

Jim Banachowski
Vice President, Eastern Region
The Andersons Inc.
Maumee, OH

Edward Milbank
President
Milbank Mills Inc.
Chillicothe, MO

Steven Nail
President & CEO
Farmers Grain Terminal Inc.
Greenville, MS

Steve Young
Grain Merchandiser
Grainland Cooperative
Holyoke, CO