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M E M O R A N D U M

TO:	Iowa Institute for Cooperatives
FROM:	Eric J. Eide
DATE:	April 22, 2020
RE:	Supreme Court decision on drying/storage charge priority over bank's UCC security interest

On April 17th, the Iowa Supreme Court released its much – anticipated decision in Heartland Coop's appeal of a Story County District Court's decision that found MidWestOne Bank's prior perfected security interest in a farmer's grain was superior to the coop's claim for reimbursement of its drying and storage charges. As a result, upon the sale of the grain, all of the proceeds were payable to the bank – without deduction for the drying and storage charges.

In a side issue, the Supreme Court did reverse the District Court's use of an expanded statute of limitations that allowed the bank to go back over 5 years' worth of grain sales. The Supreme Court ruled that the proper limitations period was 2 years from the date of sale.

With respect to the lien priority issue, the Supreme Court refused to recognize the coop's equitable argument of "*unjust enrichment*" in the face of the Iowa's statutory lien laws.

As coops digest the ramifications of the Supreme Court's decision and revise their operations accordingly, it is important to keep in mind the following points:

1. **Heartland was not able to claim any kind of statutory lien or security interest under Iowa law**. Iowa's Uniform Commercial Code has a statutory warehouse lien law (§554.7209) that *would have* governed this case *if* Heartland had either (i) a storage agreement, or (ii) a warehouse receipt for the grain in question. Without the ability to argue for any kind of lien, Heartland was left to make equitable arguments based on fairness and industry practice – and, after a thorough analysis, the Supreme Court decided in favor of the UCC's statutory framework. "*We favor allowing the UCC's priority system to provide clarity, uniformity and consistency in commercial transactions. These objectives would be undermined by allowing unjust evident claims against secured creditors"*. The Court went on to point out in a footnote the recent legislative attempts to amend the Uniform Commercial Code (UCC) in order to give elevators a priority for drying and storage charges – and were likely hesitant to venture into what could be seen as a policy issue better addressed by the

legislature. Thus, all coops should have either a written storage agreement and/or formal warehouse receipt for all customer grain in storage.

2. **The bank was able to argue that it had no actual notice the coop was deducting drying and storage charges from the proceeds checks**. It is important to remember that the District Court's decision was a summary judgment, with all evidence presented in the form of written exhibits – there was no trial or witnesses - and on appeal, the Supreme Court did not take or receive any new evidence. The Supreme Court respectively pointed out that the record had "*no evidence*" that either the producer or Heartland had ever notified Midwest One of the deductions. As a result, both the Supreme Court and the District Court found nothing in the record to show that the bank had "*actual knowledge*" of those deductions before 2017. So, despite the logical claims that any bank "*knows*" that its grain collateral is being stored and dried, or should know it when cashing the proceeds check, the lack of proof of actual knowledge by the bank was an important factor working against the coop's claim for equitable relief. Thus, all coops need to notify secured creditors of their intent to deduct customary drying and storage charges from the proceeds. Such notice should be written to coordinate with the existing provisions of the Iowa warehouse lien law.