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August 7, 2015

CASE NUMBER 2602

PLAINTIFF: **CARGILL INCORPORATED**
MINNEAPOLIS, MN

DEFENDANTS: **L&R FARMS PARTNERSHIP AND JAMES STEVEN LEWIS**
MEMPHIS, TN

STATEMENT OF THE CASE

This case involved three soybean contracts. In the fall of 2009, James Steven Lewis ("Lewis") on behalf of L&R Farms Partnership ("L&R") entered into three "No Basis Established" grain contracts to sell a total of 150,000 bushels of soybeans to Cargill, Incorporated ("Cargill"). The contracts were priced off the "Chicago Soybeans Nov 10" futures. After a data entry error of delivery date in one of the contracts was corrected, the contracts provided as follows:

Contract #	Bushels	Delivery	Price
100005	50,000	9/1/10 - 10/31/10	$9.21
100339	50,000	9/1/10 - 10/31/10	$8.9825
100342	50,000	10/1/10 - 10/31/10	$9.00

The contracts also provided for a $0.08 per bushel service fee when the contracts were entered and a $0.05 per bushel service fee at the time of settlement. The contracts further provided that the futures contract month could be amended a maximum of two times for a $0.02 per bushel service fee for each amendment. The pertinent contractual provision in this regard stated:

> Seller has the right to amend the futures contract month and year set forth above. Seller must notify Buyer of Seller's desire to roll the contract 30 days prior to the first business day of the Shipment Period. The futures level will then be adjusted by the difference between (a) the futures price in the month and year stated in this Contract and (b) the futures price in the month and year stated in the amendment. If the new futures price is higher ("carry") than the one stated in the Contract, the adjustment will be upward. If the new futures price is lower ("inverse") than the one stated in the Contract, the adjustment will be downward.
>
> The Seller may amend the futures contract month and year for the entire quantity under this Contract a maximum of two times, and then only to the next futures contract month within the crop year.

Cargill also offered grain pricing mechanisms whereby the pricing component of the contracts could be amended based upon certain market movements within a specified pricing period. In September and October of 2009, L&R entered into four different pricing mechanisms for the contracts. Cargill mailed confirmations to L&R for each of the pricing amendments that were entered. The market went against L&R on all four pricing mechanisms resulting in a loss of equity on the contracts.

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The market losses for each of the pricing mechanisms were as follows:

9/3/09	Pricing Amendment	$.013 per bushel loss
10/12/09	Focal Point Amendment	$0.1925 per bushel loss
10/15/09	Pricing Amendment	$0.665 per bushel loss
10/23/09	Focal Point Amendment	$0.08 per bushel loss

Except for the 10/15/09 Pricing Amendment, L&R closed its position during each pricing period. L&R, however, never closed the 10/15/09 Pricing Amendment allowing it to expire. For the three amendments that L&R closed, Cargill mailed confirmations showing the closing price and loss per bushel. The 10/15/09 Pricing Amendment that expired was based upon the CBOT "January 2010 SFO 1000 Put" with a pricing deadline of 12:00 a.m. Central on Dec. 24, 2009. When this pricing mechanism expired, Cargill did not mail an expiration confirmation to L&R.

From 2009 to 2010, there was a significant rally in the soybean market. The soybean market increased over $3 per bushel from late 2009 to late 2010. In October 2010, L&R had not requested that its contracts be rolled and had not scheduled delivery of any soybeans. Jeff Via ("Via") with Cargill contacted Lewis to determine L&R's delivery intentions. On October 26, 2010, Via and Lewis agreed to roll the contracts to January 2011. Cargill subsequently mailed confirmations for both the futures reference month and the shipment period rolling all three contracts to January 2011. The confirmations for the futures reference month rolls increased the price of each contract by the "carry" spread between the Chicago Soybeans Nov 10 futures and the Chicago Soybeans Jan 11 futures. L&R did not object to or question these confirmations.

On December 30, 2010, L&R had not requested that its contracts be rolled and had not scheduled delivery of any soybeans. Via again contacted Lewis to determine L&R's delivery intentions. The details of this conversation were subject to much dispute. Via contended that he told Lewis that Cargill would only agree to roll the delivery month of the contracts to March 2011 if Lewis would sign the March 11 futures reference month roll and the pricing amendment confirmations that were previously mailed to L&R. Lewis, on the other hand, contended that Via agreed to roll both the futures reference month and the delivery period on all three contracts to March 2011 without any conditions. Lewis acknowledged that Via wanted the documents signed, which Lewis said he would sign. However, Lewis denied there was any urgency or that contingencies were placed on signing documents.

Cargill subsequently mailed confirmations to L&R to roll the futures reference months to March 2011, but Cargill did not mail confirmations to roll the delivery period. There was a "carry" market, and the confirmations adjusted the contract prices by the spread between the Chicago Soybeans Jan 11 futures and the Chicago Soybeans Mar 11 futures. L&R did not object to or question these confirmations.

On January 25, 2011, Via called Lewis about getting the documents signed, and Lewis stated that he was busy. On January 27, 2011, Via was in Lewis's hometown of Brownsville, Tennessee, and attempted to make an unscheduled in-person visit to have Lewis sign the documents. When Via called Lewis to tell him he was in Brownsville and wanted to meet, Lewis was on his computer at home and told Via that he was busy and to call him next week. Lewis and Via spoke again on February 2, 2011. Lewis contended that Via asked about getting documents signed, but there was no discussion of delivery.

On February 28, 2011, Cargill unilaterally rolled the futures reference month on the contracts to May 2011. Although the contracts only allowed for two rolls, Cargill contended that it was placed in a difficult position and unilaterally made the rolls hoping that it would get something worked out with L&R on delivery. Confirmations were mailed to L&R rolling the futures contract months to May 2011. There was a "carry" market, and the confirmations adjusted the contract prices by the spread between the Chicago Soybeans Mar 11 futures and the Chicago Soybeans May 11 futures. L&R did not object to or question these confirmations.

On March 2, 2011, Cargill mailed a demand for adequate assurance to L&R setting forth total equity due Cargill in the amount of $846,500. The letter demanded payment or delivery of the soybeans by 12:00 noon on March 14, 2011, or Cargill would cancel the contracts. Lewis stated that he did not see this letter until March 9, 2011. Upon receipt of the letter, Lewis called Via asking about the events that justified Cargill's demand for adequate assurance and requested documents supporting Cargill's calculation. Lewis stated that his father had been ill, and that L&R could not make delivery by March 14, 2011.

On March 11, 2011, Lewis called Via again. During this conversation, Via asked Lewis if L&R would deliver the soybeans. Lewis responded that delivery was between him and his attorney. This same day, Cargill mailed a notice of contract cancellation to L&R demanding $799,250 in damages. Cargill's calculation was based on the difference between the current market price of $13.345 derived from the Chicago Soybeans May 11 futures and the applicable prices for each contract after netting fees and pricing amendments. Cargill included $0.02 service charges for each of the three futures month rolls and an additional $0.10 cancellation fee for the margin it would have been willing to sell the soybeans had delivery occurred. Cargill noted that the calculation presented in its cancellation notice was less than what was contained in its demand for adequate assurance due to a drop in the Chicago Soybeans May 11 futures market from March 2, 2011 to March 11, 2011.

On March 22, 2011, a meeting was scheduled between Lewis, L&R's attorney, and Cargill representatives. At this meeting, Cargill gave L&R an opportunity to deliver the soybeans, but Lewis said that Cargill was not getting any of L&R's soybeans.

The first issue presented in this dispute is whether the contracts were properly cancelled. Cargill claimed that it was justified in demanding adequate assurance and cancelling the contracts. L&R contended that Cargill breached the contracts by repudiating its verbal agreement to extend the delivery date to March 2011. L&R contended that before Cargill cancelled the contracts, L&R never stated it would not delivery the soybeans. Thus, L&R contended that Cargill was not entitled to any recovery as the breaching party.

The second issue in this dispute involves the amount of recovery if cancellation was proper. L&R contended alternatively that if the contracts were properly cancelled, Cargill improperly calculated its damages. L&R contended that under the contract provisions, Cargill should have adjusted the contract prices to the current futures market price with each futures reference month roll rather than adjust the contracts by the "spread" between the two futures months. L&R contended that the contracts never mention the word "spread", therefore making a spread adjustment improper. For example, when

Contract 100005 was rolled from Chicago Soybeans Nov 10 futures to Chicago Soybeans Jan 11 futures, there was a "carry" spread between the two futures months of $0.1175 per bushel. Cargill adjusted the $9.21 per bushel contract price by this spread to an adjusted price of $9.3275 per bushel. L&R, however, contended that on the roll date, the $9.21 per bushel contract price should have been adjusted to the current Chicago Soybeans Jan 11 futures price of $12.31 per bushel.

L&R further contended that Cargill's futures reference month roll confirmations were fraudulent because they referred to "futures level" when identifying the adjusted contract prices. L&R argued that "futures level" is a term that referred to the new futures month price, which was substantially higher than the prices stated in the confirmations. Cargill responded that the confirmations identified the "futures level" for the contracts after the futures month roll adjustments. Cargill further pointed out that the confirmations were identified by, "Pricing Type: Futures roll."

L&R also contended that Cargill was not entitled to certain fees and adjustments on the contracts. Specifically, L&R contended that Cargill was not entitled to take a $0.665 per bushel loss on L&R's 10/15/09 Pricing Amendment because Cargill never provided L&R with expiration confirmations for this pricing mechanism. L&R further contended that Cargill was not entitled to take a $0.10 per bushel cancellation fee because the contracts did not provide for it. Moreover, it contended that a $0.02 service fee on the third futures reference month rolls was improper since only two rolls were authorized by the contracts.

L&R finally contended that in calculating damages under the contracts, Cargill acted inconsistently by adjusting the contract prices using spreads on the futures reference month rolls then switching to the current futures month market price on its cancellation calculation. L&R contended that if Cargill were entitled to damages, its damages would be limited to a total of $23,625 after fees and adjustments.

THE DECISION

The arbitrators closely reviewed the evidence and arguments presented by the parties in their written submissions and at the oral hearing conducted in this case.

On the first issue of cancellation, the arbitrators concluded that Cargill was justified in demanding adequate assurance and cancelling L&R's contracts. While there was significant disagreement between the parties on what was said between Via and Lewis regarding the disputed March 2011 roll, the arbitrators determined that both the NGFA Grain Trade Rules and the evidence presented by the parties in this case supported Cargill's position. NGFA Grain Trade Rule 30(C)(3) provides that, "*Telephone, verbal or voice communication, confirmation, or notification must be confirmed by subsequent written communication*." Thus, had there been a verbal agreement to extend the delivery period to March 2011, the NGFA Grain Trade Rules required that it be confirmed in writing. It was undisputed, however, that neither party provided written confirmations for a March 2011 delivery extension.

It was also undisputed that Cargill requested that contract documents be signed on December 30, 2010, January 25, 2011, January 27, 2011, and February 2, 2011, including through an attempted in-person visit when Lewis was at home on his computer. Lewis, however, never attempted to sign the documents. Furthermore, although Lewis contended that he never told Cargill that L&R would not delivery the soybeans (until after the contracts were cancelled), the arbitrators determined that L&R did not take steps showing that L&R would make delivery. L&R never attempted to schedule delivery with Cargill, and Lewis never stated that L&R would make delivery when specifically asked. Moreover, the fact that Cargill was still willing to accept delivery after the contracts were cancelled showed that Cargill was willing to work with L&R if it had trouble meeting the March 14, 2011 adequate assurance deadline.

With regard to the second issue on damages, a major point of controversy was the manner in which the contracts were adjusted by the futures reference month rolls. Cargill adjusted the contract prices by the spread between the two futures months. L&R, however, contended the contracts should be adjusted to the new futures month price. The arbitrators determined that even though the contracts did not mention the word "spread," they described a spread adjustment. L&R offered the CME definition of "spread" to be *"the difference between the price of a futures month and the price of another futures month of the same commodity."* The contracts referred to making an adjustment by *"the difference between (a) the futures price in the month and year stated in this Contract and (b) the futures price in the month and year stated in the amendment.*" The contracts further stated that a "carry" will be adjusted upward, and an "inverse" will be adjusted downward. The arbitrators concluded these terms are indicative of a "spread" adjustment.

Although the arbitrators noted that Cargill's futures month roll confirmations could have provided more detail on how the contract adjustments were calculated and also provided more clarity in describing the adjusted contract price, the arbitrators concluded that the confirmations did not constitute a breach or fraud by Cargill justifying L&R's failure to deliver under the contracts. The arbitrators further decided that in the confirmations issued, Cargill correctly applied and calculated the contractual roll terms.

The arbitrators also determined that Cargill correctly applied the current market price in its cancellation calculation. The adjustments made on the futures reference month rolls were contractual adjustments to contract prices that were set in 2009 when the market was much lower. The contract cancellations, however, were intended to put Cargill in the position it would have been in had delivery been made. Under NGFA Grain Trade Rule 28(B)(3), where a buyer has not performed, the seller is entitled to cancel the defaulted portion of the contract at the fair market value based on the close of the market the next business day. Under this rule, Cargill was entitled to the difference between the current market price at cancellation and the applicable contract prices.

With regard to the 10/15/09 Pricing Amendment, the arbitrators decided that Cargill was not required to provide expiration confirmations and was entitled to take a $0.665 per bushel loss on the contracts. It was undisputed that L&R entered into this pricing mechanism and allowed it to expire. It was also undisputed that L&R received the initial confirmations when this pricing mechanism was entered. The confirmations identified the expiration date, and there was no dispute over how the pricing mechanism would be calculated if allowed to expire. Given these circumstances, the arbitrators concluded that the initial confirmations met the requirements of NGFA Grain Trade Rule 4, which requires written confirmation of contractual alterations.

With regard to fees, the arbitrators determined that Cargill's claimed cancellation fee of $0.10 per bushel and service fee of $0.02 per bushel for the third futures reference month roll were not authorized. The arbitrators agreed with L&R that there were no contractual provisions providing for these fees. The arbitrators further decided, however, that Cargill's unilateral third futures reference month rolls did not constitute a breach that justified L&R's failure to deliver. Rather, it was an attempt by Cargill to mitigate damages by obtaining delivery and it ultimately benefited L&R by adding equity to its contract prices. Lastly, although not raised as a point of contention by the parties, the arbitrators concluded that the contractual service fee of $0.05 per bushel to be assessed at the time of settlement was not authorized because the contracts were never settled.

THE AWARD

The arbitrators awarded a total of $773,000 in damages to Cargill calculated as follows:

Contract Nos.	**10005**	**100339**	**100342**
Initial Contract Price	$ 9.2100	$ 8.9825	$ 9.0000
Contract Entry Service Fee	$ (0.0800)	$ (0.0800)	$ (0.0800)
9/3/09 Pricing Amendment	$ (0.1300)	$ (0.1300)	$ (0.1300)
10/12/09 Focal Point Amendment	$ (0.1925)	$ (0.1925)	$ (0.1925)
10/15/09 Pricing Amendment	$ (0.6650)	$ (0.6650)	$ (0.6650)
10/23/09 Focal Point Amendment	$ (0.0800)	$ (0.0800)	$ (0.0800)
Nov 10 to Jan 11 Roll Adjustment	$ 0.1175	$ 0.1175	$ 0.1175
Jan 11 to Mar 11 Roll Adjustment	$ 0.1100	$ 0.1100	$ 0.1100
Mar 11 to May 11 Roll Adjustment	$ 0.0875	$ 0.0875	$ 0.0875
Service Fees for 2 Rolls	$ (0.0400)	$ (0.0400)	$ (0.0400)
Net Adjusted Contract Price	$ 8.3375	$ 8.1100	$ 8.1275
Market Value at Cancellation	$ 13.3450	$ 13.3450	$ 13.3450
Damages Per Bushel	$ 5.0075	$ 5.2350	$ 5.2175
Bushels	50,000	50,000	50,000
Damages Per Contact	$ 250,375	$ 261,750	$ 260,875

Each party shall be responsible for paying its own expenses associated with this proceeding.

Decided: May 1, 2015

SUBMITTED WITH THE UNANIMOUS CONSENT OF THE ARBITRATORS, WHOSE NAMES AND SIGNATURES APPEAR BELOW:

Todd Lafferty, *Chair*
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