

GETTING PAID FOR YOUR SEED

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AEE Series No. 384

April 12, 1983

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The talks you heard earlier were mainly about the production aspects of seed potato production. My talk concerns the business aspect of growing seed potatoes. The topic is one that nearly everyone in the potato industry is concerned about: getting paid. Although my talk won't show you how to solve all of your accounts receivable problems, it should give you something to think about.

Your seed potato business is unlike the businesses in town that buy goods in quantity from a wholesale market and sell a little each day in a retail market. Your business is more like a manufacturing business. You buy inputs in a retail market in the spring and put them into a production process that gives you something to sell the following year.

There is a cash flow problem inherent in your business. You started to incur expenses (e.g. fertilizer) on this year's crop last spring or winter. If you did some fall field work your expenses started even earlier. Even after you harvested your crop, you are still incurring expenses through the storage season. It is not until you actually sell and deliver some seed potatoes, up to a year later, that you actually begin to receive some income. Buyers that are slow in paying, make the cash flow problem even worse.

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\*Presented at the Idaho Seed Potato Growers Seminar, Pocatello, Idaho, November 18, 1982.

It takes a good manager and financial planner to make the best of this cash flow situation. Good businessmen are aware of the time value of money. Time is money. When you get paid, is sometimes as important as how much you get paid.

There is a cost associated with the use of money. It is not a free good. Just ask your banker. When someone owes you money and is not paying interest you are bearing the cost of that money.

Most seed potato growers need to borrow operating money. You know what that cost is; it is the interest rate the lender charges you. The sooner you get paid, the sooner you can pay the lender and reduce the cost of money.

If you are one of the fortunate few that doesn't need to borrow money, there is still a cost for the money you have tied up in your crop. If you had that money in cash you could invest elsewhere, such as a bank CD, or a money market mutual fund, or your own business. I remember one year when a farmer could buy fertilizer in the winter for 30% less than he could in the spring. That was an opportunity to earn a 30% return on an investment in the fertilizer needed to plant the next crop. Whenever you don't have access to your money you are losing investment opportunities and returns that could be yours.

Let's consider an example of a farmer that uses some of his own money and some of the bank's money to grow seed potatoes. Assume that he borrows 60% of the money he needs at 17%, which was about the rate last spring. Also assume that the remaining 40% is his own money which he could have invested elsewhere at 11%. The calculations reveal that his average cost of money is 15%.

Suppose the seed grower in this example is offered \$7 for his seed in November. Since you know that there is a cost to money, you know that if he received the \$7 now it would be more valuable than \$7 received months from now.

Table 1 shows what the \$7 is worth today according to when the grower gets paid. If the sale was made today, and the buyer also paid today, the \$7 is really worth \$7. Since that is unlikely, it is interesting to do what many businessmen do--convert future dollars to a present value.

Table 1 shows that if the seed grower gets paid in six months (i.e. next May), that \$7 seed is worth only \$6.48 today in November. If the buyer waits until after he harvests and sells his crop to pay (12 months), the present value of that \$7 seed is only \$5.95.

TABLE 1

PRESENT VALUE OF \$7 SEED COST OF MONEY = 15%

<u>Month Paid</u>	<u>PV No DP</u>
2	\$6.82
4	6.65
6	6.48
8	6.30
10	6.12
12	5.95

If any of you growers want to make a table like this for your own situation, I will briefly review how I made the calculations. First you need to determine your cost of money which may be the average of what you borrow at, and the rate at which you could invest. Next, divide by 12 to get a monthly cost of money. Then, multiply by the number of months

until payment. Subtract this figure from the sales price and you have present value price.

Besides having a written contract provision for interest charges on late payment, you can also improve your present value price by arranging for a down payment. Many seed growers have down payment specifications in their contracts. A written seed contract is something that all seed growers should consider. Mike Koehnke of Townsend, Montana spoke to this group last year about the Universal Seed Potato Contract he helped draft. This contract has provisions for making up to two down payments.

It is highly unlikely that a buyer would pay you now in full for seed he won't plant until next spring (unless he has an income tax problem this year). However, if you can get a portion, in the form of a down payment, you are much better off.

Table 2 is the same as the previous table except that an extra column has been added. That column shows the present value price when the seed grower gets a 30% down payment (\$2.10). Notice that if the grower gets paid the balance next May (6 months) he is 15¢ per hundredweight better off with the down payment. If he gets paid in 12 months the difference is 31¢ per hundredweight. The figures would look even better if a larger down payment or an additional down payment were arranged.

There is another business aspect of your operation that can cost money--late shipment. When I was growing seed potatoes in Wisconsin we would have buyers take delivery a month or two later than we had agreed. Besides the cost of late payment the seed grower also incurs the cost of additional shrink which may be 1% per month or more.

TABLE 2

PRESENT VALUE OF \$7 SEED COST OF MONEY = 15%

<u>Month Paid</u>	<u>PV No DP</u>	<u>PV 30% DP</u>
2	\$6.82	\$6.88
4	6.65	6.76
6	6.48	6.63
8	6.30	6.51
10	6.12	6.39
12	5.95	6.26

On top of those costs you might have the cost of additional labor. This could happen when shipment is delayed so long that you are grading seed and planting your crops at the same time. Most operations would need to hire extra help in such a situation. The total cost of delayed shipments can run 2 to 3% or more each month.

I'm sure that you seed growers have thought about the costs of late payment, even if you haven't seen it expressed in dollars and cents. What are some things that you can do to get the most for your price? My opinion is that you should have a written sales contract with provisions for (1) down payment; (2) interest charge for late payments (the rate should exceed your cost of money); and (3) an additional charge for late shipments (this is not included in the Universal Seed Potato Contract).

You can also make use of something called a seed lien, which I will soon discuss in detail. Before that, however, let's think about something called good will. Since repeat customers are so important in the seed business, you need to establish a good relationship with your customers and not offend them. If you have been selling seed to an excellent customer for 20 years, and for some reason he is a little late in paying one year,

he would probably be offended if you slapped a seed lien on him. Save the seed liens for the customers you can afford to lose, or the ones you know to be financially unstable.

Now let's see what seed liens are all about. I have never filed a seed lien and I am not an attorney, so you may have some questions that I can't answer. However, I have done some homework. I researched the Idaho Code and some other law books, went to the County Recorder where seed liens are filed, and asked several attorneys a bunch of questions.

First, you may want to know the purpose of a seed lien. It is a legal instrument that, if used properly, can assure that a seed potato grower gets paid when the buyer sells the crop he grew from that seed.

The priority of the seed lien is also important. That is, if there is a long line of people waiting to get paid, where is the seed lien's place in that line. The seed lien is a good deal in Idaho. It is at the head of the line except for farm laborer's liens which aren't too common. This means that you get your money even before the bankers get theirs.

There are, of course, regulations that need to be followed for a seed lien to be legally binding. The time of filing is of extreme importance. The seed lien must be filed with the County Recorder, in the buyer's county, within 90 days after the seed is delivered. Therefore, you should keep track of who owes you money, when you delivered, and the filing deadlines.

For the seed lien to be legitimate, the Idaho law states that it must include certain information. Necessary information includes:

1. Names of all parties
2. Seed amount, type and price
3. Delivery date

4. Legal description of the land where the buyer planted your seed and a description of the crop (e.g. russet burbank potatoes planted on the SW 1/4 Sec 2 of X Township).
5. Verification of your claim by the signature of an Attorney or Notary Public.

There is a question that naturally comes up but is not covered in the Idaho seed lien law. That question is, "should I notify my customer that I have placed a seed lien on his crop?" I am acquainted with an Idaho Falls attorney that filed a lien this year. He sent a certified letter to the customer stating that a lien had been filed on his crop and that legally he could not sell his crop without the lienholder's written consent, which is correct. They got paid one week after the letter was mailed. Although notifying the customer is not necessary, and doesn't guarantee immediate payment, it certainly seems like a good idea.

There is another point of Idaho seed lien law of which you should be aware. The seed lien is only good for six months after the buyer harvests his crop. Of course, a lot of potato growers store their potatoes for more than six months. As the end of this period approaches, and the seed grower hasn't been paid, he needs to think about 'enforcing' the lien. This is where the seed grower forces the buyer to sell enough of his crop to pay for the seed. Often the buyer may be uncooperative and the court may appoint a third party to sell the potatoes. The seed grower can also collect additional money to cover interest, legal fees, and marketing costs.

If the customer sells his potatoes and you still aren't paid, legally you can collect from the firm that bought his potatoes. The Idaho law places the burden of checking for liens on the buyers. The reasoning is that it is easier for buyers to check for liens at the County Recorder's



office than it is for the lienholder to contact all potential buyers. If the buyer is, in fact, aware of the lien he must pay you first.

There is one more aspect of seed liens which may be of interest to you. That is, can you file a seed lien on a buyer that is in another state? It depends on the law in that state; Idaho's law does not apply. You would probably need to contact an attorney in that state. Even if that state has a seed lien law, the provisions may be slightly different. For example, maybe you need to file the lien within 75 days of delivery rather than 90 days.

I haven't contacted attorneys in other states but the Idaho Code mentions two states that have similar seed lien laws. Washington is one of those states. Although very little Idaho seed goes to Montana, that is the only other state mentioned. Oregon and Nevada are not mentioned.

I have provided handouts for those seed growers interested in further information on seed liens. The first page is a copy of a barley seed lien filed in Bonneville County (seed liens are public information). The next two pages are a copy of the Idaho seed lien law as it appears in the Idaho law books.