Approved: 3-5-96
Date

MINUTES OF THE HOUSE COMMITTEE ON AGRICULTURE.

The meeting was called to order by Chairperson Joann Flower at 9:00 a.m. on February 23, 1996, in Room 423-S of the Capitol.

All members were present except: Representative Crabb - Excused
Representative Humerickhouse - Absent

Committee staff present: Raney Gilliland, Legislative Research Department
Jill Wolters, Revisor of Statutes
Kay Scarlett, Committee Secretary

Conferees appearing before the committee:
Jamie Clover Adams, Kansas Grain and Feed Association

Others attending: See attached list

Minutes of the February 20, 21, and 22 meetings were distributed. Members were asked to notify the secretary of any corrections or additions before 5:00 p.m. today or they will be considered approved as presented.

Jamie Clover Adams, Kansas Grain and Feed Association, presented the report on the potential merger of the Grain Inspection Department with the Kansas Department of Agriculture as requested by the 1995 Interim Special Committee on Agriculture and Livestock. (Attachment 1) The study committee consisted of representatives from the Kansas Cooperative Council, Kansas Department of Agriculture, Kansas Grain Advisory Commission, and the Kansas Grain and Feed Association. They were to study three issues:

1. The perceived regressivity of warehouse license fees;

2. The appropriate number of warehouse audits per year; and

3. The possibility of merging all or part of the functions of the Kansas Grain Inspection Department into the Kansas Department of Agriculture, as well as privatization of the KGID Inspection Division.

Gary Bothwell, Director, Grain Inspection Department; Ron Scheibmeir, Grain Inspection Department; Shirley Strnad, United Grain, Inc., Belleville; David Warrington, Collingwood Grain, Inc., Hutchinson; and Tom Tunnell and Jamie Clover Adams, Kansas Grain and Feed Association, answered committee questions.

The meeting adjourned at 10:00 a.m. The next meeting has not been scheduled at this time.

HOUSE AGRICULTURE COMMITTEE GUEST LIST

DATE: Feb. 23, 1996

NAME	REPRESENTING
Jamie Clover Adams	KGFA
Barb Hinton	Post Audit
Joe Lieber	KS Co-op Council
Marvin [illegible]	Webb & associates
David J [illegible]	Collingwood Grain
Roy [illegible]	Kans. Grain Insp. Dept.
Shirley [illegible]	United Grain
Phyllis Strand	United Grain Inc
Gary M. Bothwell	Grain Inspection
Leslie Kaufman	Ks Farm Bureau
Tom Tunnell	KGFA
Greg Krissek	KS Dept of Ag
Rich McKee	KLA

Report
to the Standing
House & Senate Agriculture Committees
as requested by the
Interim Special Committee Agriculture & Livestock

February 1, 1996

Parties to the Report: Kansas Cooperative Council
Kansas Department of Agriculture
Kansas Grain Advisory Commission
Kansas Grain and Feed Association

House Agriculture
Attachment 1
2-23-96

The following report is submitted to the House and Senate Agriculture Committees at the request of the 1995 Interim Special Committee on Agriculture and Livestock.

Background

In October 1995, the Kansas Legislature's Special Committee on Agriculture and Livestock held a hearing focusing on the financial position and regulatory responsibilities of the Warehouse Division of the Kansas Grain Inspection Department (KGID). The Inspection Division was also discussed. After deliberation, the Special Committee recommended that a study be conducted to examine three issues. These included: (1) examination of the warehouse license fee schedule to address concerns over the perceived regressivity of fees; (2) examination of a risk-based model to determine the appropriate number of warehouse audits per year, and; (3) the possibility of merging all or part of the functions of KGID into the Kansas Department of Agriculture (KDA), as well as privatization of the KGID Inspection Division. The Special Committee concluded that the study group should consist of members of the Grain Advisory Commission*, the KDA, as well as the industry trade associations. The Special Committee requested the study group report its findings to the standing Senate and House Agriculture Committees by February 1, 1996. The Grain Advisory Commission, KDA, the Kansas Coop Council and the Kansas Grain and Feed Association (KGFA) met at the KGFA offices in late November and mid-January to address these issues.

Warehouse License Fee Schedule

The study group** discussed warehouse license fees and their relation to firm size. The current license fee schedule provides for a graduated fee assessment based upon the bushel capacity of the elevator. Legislative committee members expressed concerns that the fee schedule was regressive since when the license fee is expressed in relation to warehouse capacity, the per bushel fee is greater for smaller elevators.

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* The five member advisory commission is appointed by the Governor. It consists of a farmer, a banker, a terminal elevator representative, a country elevator representative and a cooperative elevator representative.

** KDA did not participate in this discussion since they felt they had no direct involvement in this issue.

Upon review, the Commission, KGFA and the Coop Council concluded that while the cost per bushel for smaller elevators may be higher, fixed costs must also be considered. The Warehouse Division reported that there is a fixed cost associated with each audit which remains nearly constant regardless of elevator size. The only significant difference in the audits of varying size elevators appears to be in the number of bins which must be measured and the number of transactions that must be reviewed. Consequently, an elevator with 500,000 bushel capacity and an elevator with 2 million bushel capacity have the same base fixed cost. If this base fixed cost were subtracted from the warehouse license fee -- the study group believes that each warehouse should pay the base fixed cost associated with a warehouse audit -- the cost per bushel for smaller elevators would decrease and the cost for larger elevators would increase relative to each other.

All parties agreed the current graduated warehouse license fee schedule is appropriate.

<u>Risk Assessment Model</u>

The study group** explored the feasibility of using a risk-based, statistical sampling approach to warehouse audits. Currently, state statute mandates that each state-licensed grain warehouse be examined at least once every 12 months. Upon review of the staffing needs currently required to perform an examination, it appears that extending the frequency between audits also lengthens the time needed to perform the audit. It appears this proposal offers little, if any, potential for expense reduction within the Warehouse Division. Second, some elevators must be examined more often than the statute requires because of their financial situation. This would not cease under a risk-based approach. Finally, it appears consumer protection might be compromised or at least be perceived as compromised if the frequency of examinations is reduced.

All parties agreed the current requirement for a warehouse audit every 12 months is adequate. A switch to a risk-based system would provide negligible savings and could have a significant negative impact on consumer protection.

Merging KGID with KDA

The study group explored the feasibility of merging current KGID functions into the Department of Agriculture. Several staff level meetings took place throughout the fall between KGID, KDA and trade association staff to examine this issue. Staff found that little, if any excess human resource capacity is available in KDA to competently perform the services currently offered by KGID. So, a merger would require the wholesale transfer of KGID with no staffing or duty elimination. Further, highly trained staff is necessary to carry out the warehouse audit function which is responsible for ensuring that producer grain -- valued at more than $1.13 billion annually -- is stored securely in a financially stable warehousing operation. KGID Inspection Division personnel are responsible for official grades necessary for the orderly trading of grain throughout the country and abroad.

Staff also compared KGID Warehouse Division activity and expenses to those of the Agriculture Commodities Assurance Program (ACAP) within the Division of Inspections at KDA in an effort to gage the efficiency of the Warehouse Division. ACAP was chosen for comparison because it also performs inspections in agricultural establishments. The KGID Warehouse Division and KDA ACAP are both fee funded programs with similar sized budgets and staff.[***] Both have eight (8) field people in the Agriculture Inspector II or III category. The per employee cost is $49,516 at KGID and $48,711 at ACAP which includes all costs associated with running these programs. There is only a slight difference -- 1.65% -- between total FY95 costs. The study group felt this minor variance is accounted for in the difference in longevity between the two entities -- 16 years in the Warehouse Division compared to an average of 14 years within the ACAP program. Further, other differences in cost may be explained by the detailed nature of warehouse audits. In fact, an ACAP inspector can perform several inspections within one day at more than one site. This is not the case with KGID warehouse auditors.

[***] KGID has 11 employees and spent $544,675 in FY 95. ACAP has 12 employees and spent $584,530 in FY 95.

The study group concluded that simply shifting all of the current functions of KGID to KDA would not result in substantial cost-savings to the state. Further, both KGFA and the Coop Council would oppose such a move.

Privatization of Grain Inspection

KGID is the agency designated by the Federal Grain Inspection Service (FGIS) to perform official grading services in Kansas. KGID's designation must be renewed every three years. The current designation expires in August, 1997. Currently, eight coastal states are FGIS delegated (FGIS does the work in those states) and ten states are designated (like Kansas). The remainder of the country is covered by 48 different private agencies.

KGID Inspection Division privatization discussions have surfaced primarily because of changes that occurred in the industry over the past 10-15 years. These changes -- government acreage idling programs and rail abandonment -- had and continue to have a profound impact on the structure of the grain industry and what it needs from KGID. Unfortunately, KGID was unable to effectively respond to these changes within the industry due, in large part, to their status as a state government department. Work rules, rule and regulation requirements to set fees and provide services, and politics hamper KGID's ability to respond to industry needs. However, as nearly always happens, the industry was able to fill the void by creating new entities to meet their needs -- unofficial agencies and in-house grading. These new avenues to obtain grain grades and the shrinking harvest greatly impacted the bottomline of KGID. It is these factors that led many to contemplate privatizing the inspection portion of KGID so that the future needs of the entire industry, not just those in high volume locations could be met.

The study group agreed that price and high quality service are the key factors in grain inspection no matter what entity is the FGIS designated service. While KDA agrees with this statement, they also believe privatization could potentially provide cost savings in terms of dollars and FTEs to the state. However, while privatization will take FTEs off the state rolls, the KGID Inspection Division is financed totally by fees. Given these factors, the group agreed that privatization may be necessary in the future but everyone expressed confidence in the current Director and felt with the proper tools he could keep KGID competitive. A legislative package has been introduced in the 1996 Session that should assist the Director in staying competitive. These include retaining the interest on the fee fund and removing the inspection fee setting process from the formal rule and regulation system. The trade associations are also exploring ways to assist in equipment acquisition.

The study group spent a great deal of time discussing the various components of privatization. First, the entire state must be kept as one territory to ensure that producers and grain facilities across the state receive equal service. For example, in Nebraska, the state is divided into three separate territories. Second, the FGIS designation should go to a not-for-profit entity with the best interest of the entire industry at heart. It is imperative that the high level of quality service that is currently being provided continue to ensure that the position of the grain industry will not be compromised in any manner or at any level. Third, existing equipment and reserves bought and paid for with industry funds must go with the new entity. Finally, personnel issues must be addressed.

Conclusions

The study group spent a great deal of time, energy and resources exploring the issues outlined above. We hope this analysis will be helpful to the Committees as they move forward and address these important issues.