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for the preparation of a Legal Guide  
on Contract Farming**

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**Preparation of a Legal Guide on Contract Farming –  
A preliminary outline of issues**

*(prepared by the UNIDROIT Secretariat)*

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**Introduction**

1. The practice of producing under a contract developed in the industrialised countries several decades ago especially in the livestock production sector, and is now used for many agricultural commodities in all countries of the world. Under contractual arrangements entered into with agricultural producers, food processors and distributors organise the production process in accordance with their needs, from the supply of inputs until the delivery of the produce. It is used to increase and diversify the availability of products on local and global markets and may work as an efficient tool to strengthen farmers' capacities. Contract farming is expanding in developing countries where it opens significant opportunities of economic and social development by providing local producers with access to markets and support in the form of technology transfer and credit facilities. It is further seen as a potential tool for reducing poverty, contributing to rural development and increasing food security.

2. Strengthening and improving relationships between farmers and the market on a sustainable basis is among the priority objectives in the agenda of many multilateral organisations, bilateral cooperation agencies and non-governmental organisations which work to support the agricultural sector in developing countries. Within the United Nations system, the Food and Agriculture Organization (FAO) and the International Fund for Agricultural Development (IFAD) are paying increased attention to the establishment of a conducive environment to promote the inclusion of small-holder farmers in agricultural value chains. Contract farming is bound to attract significant attention in the context of the current preparation of *Principles for Responsible Agricultural Investment* ("RAI Principles") within the Committee on World Food Security.

3. Contract farming arrangements reflect multiple commercial practices and their success depends on many elements. The legal framework plays a particularly important role in view of the complex nature of the relationship where parties are linked through a variety of obligations with different levels of risks and benefits. An additional feature is the typical disparity in economic and bargaining power between producers who are generally vulnerable parties - especially so for small farmers in developing countries – and contractors, often large food processing and marketing companies, which may lead to imbalanced or exploitative situations.

4. In most countries contract farming arrangements are regulated under the provisions of general contract law. In a few countries, ad hoc legislation has been enacted which identifies a special contractual type and contain provisions applicable to certain aspects of the relationship, mainly to protect producers against unfair practices, and to establish dispute resolution mechanisms intended to provide adequate enforcement of contracts and enhance voluntary compliance.

5. As indicated in the World Investment Report 2011,<sup>1</sup> guidelines, checklists of issues to be considered in negotiations, codes of conduct, model contracts for contract farming can be an effective tool for Governments to help strengthening the negotiating power of domestic firms and achieving a fair sharing of risk between the parties. In this connection, international “soft law” instruments can promote contract farming by harmonizing the rules governing the contractual relationship between private parties or by guiding private parties in drafting the contract.<sup>2</sup>

### ***Objectives of the future UNIDROIT Guide on Contract Farming***

6. The purpose of the envisaged UNIDROIT Guide would be to spread knowledge with a view to providing all those who deal with contract farming, whether they be agricultural producers or market operators, lawyers, judges, arbitrators or scholars, with a tool for the better understanding of the possibilities it offers.

7. In particular, the future Guide could be of assistance to parties – and their legal counsels – in negotiating and drawing up contract farming arrangements by identifying the legal issues involved in those agreements, discussing possible approaches to the issues and where appropriate, suggesting solutions which parties may wish to consider. By furnishing comprehensive information the future Guide is aiming at filling the informational gap between the parties, which would otherwise have placed one of them at a disadvantage. It should therefore contribute to providing the parties with greater confidence in dealing with contract farming.

8. The future Guide could help identify solutions for drafting fair and commercially sound contracts serving as a guide to “good contracting practice”. As such, it could provide a useful tool in the context of dispute resolution mechanisms, in particular in alternative resolution proceedings, to supplement the existing legal framework when it proves insufficient.

9. The future Guide could also serve as a reference document for law makers and public authorities dealing at a public policy level with contract farming. It could help in assessing the possible need for and content of a specific legislation on contract farming. It could be used as a reference in the context of legislative or regulatory reforms, also by contributing to a harmonized and fair approach to the legal regime of contract farming arrangements at a time when markets are increasingly global and integrated.

10. In view of its various potential applications, the future Guide could provide an additional tool available to international organisations and bilateral cooperation agencies as well as non-governmental organisations engaged in strategies and programs in support of contract farming in developing countries.

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<sup>1</sup> World Investment Report 2011 (UNCTAD): *Non-Equity Modes of International Production and Development*, p. 171 et seq.

<sup>2</sup> This was in essence the purpose of UNIDROIT in preparing a Guide for another form of non-equity investment, *i.e.* the *UNIDROIT Guide to International Master Franchise Arrangements* (2nd Edition 2007) – p. xxxi-xxxii.

## I – Notion of Contract Farming

### A – Economic approach

11. The term “contract farming”<sup>3</sup> has been described as referring to “a particular form of supply chain governance adopted by firms to secure access to agricultural products, raw materials and supplies meeting desired quality, quantity, location and timing specifications”.<sup>4</sup>

12. Under an extensive interpretation, contract farming may cover a broad array of different agreements: “market specification” contracts which guarantee farmers with a marketing outlet and time of sale, and possibly a price structure, on the basis of a specified quantity and quality of produce; “resource-providing” contracts where the purchaser also provides certain physical or technical inputs; “production management” contracts where the purchaser stipulates and enforces conditions of production and farm-based processing.

13. Under a more restricted approach, contract farming “[...] invariably involves the purchaser in providing a degree of production support”.<sup>5</sup>

### B – Variety of legal forms

14. The first kind of agreement potentially covered by the broad economic definition of contract farming, *i.e.* “market specification contracts” does not in principle raise particular issues as regards the legal nature of the relationship. As they are described, such contracts fall squarely under the typical structure of the sale/purchase transaction – consisting in an exchange of goods against a set price –, which is the paradigm form of special contracts. The legal form allows for different business formats: in particular, under forward delivery contracts, producer and buyer agree on the future delivery of determined (already produced, being produced or to be produced) goods, at a

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<sup>3</sup> Also referred to as *i.a.* “Producing under a contract”, “contractual agriculture”, “agribusiness contracts”.

<sup>4</sup> Cf. Da Silva, C., (in *The growing role of contract farming in agri-food Systems development: drivers, theory and practice*, Agricultural Management, Marketing and Finance Service FAO, Rome, 2005) “Regardless of the typology, the general term “contract farming” refers to a particular form of supply chain governance adopted by firms to secure access to agricultural products, raw materials and supplies meeting desired quality, quantity, location and timing specifications.” ... “Contracting is an intermediate mode of coordination [between spot markets or open markets, and full vertical integration where a firm exercises centralised ownership control over two or more different stages in a chain], whereby the conditions of exchange are specifically set among transaction partners by some form of legally enforceable, binding agreement. The specifications can be more or less detailed, covering provisions regarding production technology, price discovery, risk sharing and other product and transaction attributes”.

<sup>5</sup> Cf. Eaton, C. and Shepherd, A. (in: *Contract Farming: Partnerships for Growth*. FAO Agricultural Services, Bulletin 145, Rome, 2001): “Contract farming can be defined as an agreement between farmers and processing and/or marketing firms for the production and supply of agricultural products under forward agreements, frequently at predetermined prices. The arrangement also invariably involves the purchaser in providing a degree of production support through, for example, the supply of inputs and the provision of technical advice. The basis of such arrangements is a commitment on the part of the farmer to provide a specific commodity in quantities and at quality standards determined by the purchaser and a commitment on the part of the company to support the farmer’s production and to purchase the commodity”.

For a summary of approaches and definitions, Prowse, M., *Contract Farming in Developing Countries – A Review*, Agence française de développement, 2012, pp. 9-12.

predetermined price and other agreed conditions.<sup>6</sup> It may be noticed however that as part of their public policy to support the agricultural sector and better organise the supply chains of agricultural products, many countries have adopted special regulations dealing with the required form and content of the agreements between producers and buyers.<sup>7</sup>

15. Under the other two kinds of agreements designated as “resource-providing” and “production management” contracts, both parties undertake to make performances relating either to goods or to services: both farmer and contractor participate in the production activity, to a lesser or greater extent and in a variety of forms. The combination of the obligations of the parties involved in achieving the economic purpose of the overall transaction represents the complex and original legal nature of this kind of commercial transaction.

16. It is accordingly submitted that the future UNIDROIT Guide should focus on this particular transaction, hereafter designated as “agricultural production contract”.<sup>8</sup>

## II – The agricultural production contract

### A – Common features of agricultural production contracts

17. While transactions vary depending on the particular commodity or service concerned, the geographical location, type of parties etc., they present the following most common features:

- farmer provides the land, fixed installations, equipment and labour and agrees with contractor to grow or raise and deliver a specified product for a fixed term, which corresponds at least to one production cycle. Typically, the farmer enters into an exclusive relationship with the contractor;

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<sup>6</sup> Spot market transactions which most frequently take place at wholesale markets do not fall under this description as they provide for immediate delivery, while trading in certain commodities taking place on commodity exchanges under futures contracts are subject to special regulations.

<sup>7</sup> Examples of recent legislation include:

– In Spain law 2/2000 on standard contracts of agrifood products (*Ley 2/2000 sobre contratos tipo de productos agroalimentarios* and implementing *Real Decreto 686/2000*).

– In Italy law No. 102/2005 for the Regulation of agrifood markets (“*Regolazione dei mercati agroalimentari*”) dealing with framework contracts “for the production and delivery of crop and husbandry” (“*contratto di coltivazione, allevamento e fornitura*”).

– In France: The law for the modernisation of agriculture of 27 July 2010 (*Loi de modernisation de l’agriculture LMA*) (articles L.631-24 to L.631-26 *Code rural*), applies to “contracts of sale of agricultural products to be marketed or processed”.

<sup>8</sup> Agricultural production contracts are increasingly studied under the legal viewpoint, especially in countries where a special legislation was adopted to regulate this particular contract form. For an analysis of US legislation and practice, see Hamilton, N.D., *Farmer’s Legal Guide to Production Contracts*, University of Arkansas, 7 (1995); *Idem*, “Agricultural Contracting: A U.S. Perspective and Issues for India to Consider”, in A. Gulat, P.K. Joshi and M. Landes (eds.), *Contract Farming in India: A Resource Book* (2008). The National Agricultural Law Center (in cooperation with the Drake Agricultural Law Center at Drake University School of Law in Des Moines, Iowa) has developed an internet resource center (with access to statutes and regulations, case law, bibliography and research material and other references) accessible at : <http://www.nationalaglawcenter.org/readingrooms/productioncontracts/>

At the international level, the Food and Agriculture Organization (FAO) is devoting increased attention to the international trends towards tighter alignment in agrifood supply chains, and provides information and technical support on planning and implementing contract farming operations. The internet resource center also provides access to sample farming contracts. See <http://www.fao.org/ag/ags/contract-farming/index-cf/en/>

- contractor frequently designates and may also provides specified inputs: typically seeds and fertilizers for crop productions, and animals, animal feed and veterinary products for husbandry. Depending on the underlying structure of the agreement, the producer owns the produce and sells it under agreed delivery terms to the contractor. Frequently, the producer undertakes to deliver – and contractor to acquire – the whole production. Or the contractor is the owner of the raw material (typically seeds or plants and small animals) and keeps the ownership throughout the production process involving growing the crop or raising poultry or livestock;
  - contractor frequently prescribes and producer undertakes to comply with certain specified processes and techniques during production; contractor may provide training and extension services in relation to production techniques and would perform supervision and oversight on the land or premises of the farmer. Contractor may also perform direct services in relation with the production process such as soil preparation, harvesting and other ancillary services such as transportation of the goods;
  - the price is determined under a variety of forms: it transfers value and allocates risks.
18. Alternatively – or additionally - firms may also be placed upward in the supply chain, and would work as suppliers of inputs (typically seeds and animal feed) to the farmer.

### **B – Principal benefits arising from the use of agricultural production contracts**

19. For industrial and commercial firms in the food processing and marketing sector, engaging in agricultural production contract serves as a tool to better organise its typical economic purposes. The contract secures a supply of product meeting designated quality features – also for traceability purposes in the context of food safety requirements –, in optimised quantities and in convenient time in accordance with the objectives of such firms. Firms can have access to production capacities without investing capital in fixed assets – and without having to bear the related liabilities. They can also protect their intellectual property rights over special improved varieties of crops at all stages from development to marketing.
20. For producers, agricultural production contracts secure an income generating activity through the access to markets, including specialised markets which offer opportunity for obtaining higher prices. Contracts also work as a credit vehicle when the inputs are provided by the firm (as an advance payment over future delivery, or as working capital for animals owned by the firm) and as collateral to obtain credit from banking institutions. Through technical assistance provided by the contractor, farmers may acquire improved production skills.

### **C – Common problems associated with agricultural production contracts**<sup>9</sup>

21. Disparity of economic power between the parties is one characteristic feature of the relationship. Typically, large processing or marketing companies with sophisticated management capacities deal with large numbers of small or medium-scale producers thus spreading risks of loss, while producers are dependent upon natural factors and financial constraints, and lack market information. Producers are generally engaged in an exclusive relationship with the firm, and may have little or no opportunity to contract with another potential party. In certain situations where the farmer is totally dependent upon the firm, the relationship may be found to be rather of an employment nature.

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<sup>9</sup> For a general review, in particular regarding the practice in developing countries, see Pultrone, C., "An Overview of Contract Farming: Legal Issues and Challenges", *Uniform Law Review* 2012-1/2, pp. 263-289.

22. This feature has important consequences at the time when the parties agree on their obligations. The contractor is well placed to draft the contract at its own advantage while the producer may not be in a position to actually see (for oral agreements), fully understand (because of overly complex or ambiguous drafting), negotiate (for standard forms), or fully assess the extent and implications of the obligations that will bear upon him. Contractors may impose conditions that would result in a risky and onerous venture for the producer: important capital investment may be required from the producer while related repayment obligations may involve a longer period than the actual duration of the contract; through contract provisions, contractor may include terms subject to unilateral determination, waive certain warranties or liabilities and shift important risks upon the producer, for example for production loss as a result of force majeure events even where the producer does not own the goods.<sup>10</sup>

23. Also during contract performance, voluntary breaches can take place whereby parties attempt to obtain more benefits or escape liabilities. On the contractor's side this may happen for example by manipulating the performance of the producer through its own deliveries, or applying a discretionary power in refusing the produce based *e.g.* on alleged defaulting quality. On the producer's side, frequent practices are diverting the contractor's inputs or selling the production in violation of the contract. Such practices are particularly likely to occur when conditions change between the time the contract is entered into and the delivery of the goods, in particular as regards price and market conditions. When parties have not contemplated a flexible price formula or the possibility to adapt the contract, depending on the available legal remedies and enforcement mechanisms, contract breach may appear as economically more advantageous than performance.

24. In developing countries where contract farming is increasingly applied with expected benefits to increase production output, improve supply for markets and generally contribute to economic and social development, exacerbated problems may arise in the context of agricultural production relationships especially with small scale farmers.<sup>11</sup> Factors such as unsecure land tenure rights, diffuse food insecurity, high level of illiteracy, the prevalence of informal relations contribute to exposing producers to a high uncertainty regarding their obligations and their rights, with the risk of being subject to inequitable conditions and exploitative behaviours. Particularly critical issues<sup>12</sup> have been pointed out regarding farmer's compliance with domestic labour legislation, adverse effects of use of inputs for human health and the environment, the risk of farmers being ever more indebted and trapped into the contractual arrangement due to the monopolistic power of the contractor and abusive practices in particular as regards price calculation. Even where protective legal rules exist, obtaining relief through public enforcement mechanisms is often impracticable.

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<sup>10</sup> See for example the motivation appearing in the introduction to the Iowa Act "The combination of rapid consolidation in agriculture and the rise of widespread contracting in agriculture gives rise to concerns of unequal information, unequal bargaining power, and the potential for anti-competitive practices. The experience in the highly concentrated poultry industry demonstrates that abusive practices can be imposed on producers in connection with contracts. Retaliation, coercion, and discrimination against poultry producers is all too common [...]".

<sup>11</sup> Cf. *i.a.*, Eaton, C. and Shepherd, A., *supra* note 5 and Prowse, *supra* note 5.

<sup>12</sup> From a human rights perspective, see the *Interim report of the Special Rapporteur on the right to food*, Olivier De Schutter, submitted by the Secretary General of the United Nations to the Sixty-sixth session of the United Nations General Assembly, A/66/262, 4 August 2011.

### III – The legal regime applicable to agricultural production contracts

#### A – Different domestic law approaches in the definition of the applicable legal regime

25. As evidenced above, in a typical agricultural production relationship the parties undertake a variety of reciprocal and connected obligations. This raises the question of how those obligations are regulated under domestic law. Consideration of the different approaches followed in domestic law for the characterisation of agricultural production contracts is important in determining the scope of the future Legal Guide, since it helps defining the kind of agreement to which the Legal Guide is supposed to apply. Furthermore, it will impact on the question of what role should be played by the parties' autonomy in shaping their contractual relationship and in establishing a good balance between default rules and mandatory provisions.

26. Defining the applicable legal regime involves characterising the contractual relation as possibly falling under one particular legally defined contract type. While parties can designate a particular type to structure to apply to their whole relation, or to a certain part of it, they would not be entitled to choose a form inconsistent with the economic purpose they have themselves defined. A legal characterisation also involves consequences regarding aspects outside the contractual agreement, such as the tax regime.

27. As opposed to "simple" transactions where one legal category is established according to the main obligation involved, for complex relationships with more than one characteristic performance, different approaches may apply. In certain instances, on account of its original features, the law itself may establish a regime applicable to that particularly identified ("nominated") transaction. Under other legal systems, the complex nature of the relationship may lead to identify different underlying contractual structures – each identified by a different characteristic performance - with the result that the overall relationship will be subject to a combination of contractual regimes. This would be done either in consideration of the economic purpose of the transaction or as if the identified contracts were unrelated. Under a simpler, straightforward approach, one particular performance will be considered as prevailing in the transaction resulting in the application of the corresponding legal regime to the entire relationship. It must be noted, however, that even when a specific legal regime concerning agricultural production contracts is present, not all aspects of the relationship<sup>13</sup> nor all types of production contracts are necessarily covered by the special legislation (e.g. a particular commodity may be covered<sup>14</sup>) thus leaving room to the application of other approaches.

#### B – Interplay of special contractual regimes in regulating agricultural production contracts

28. A variety of special forms may become relevant in the context of agricultural production contracts. The most common forms are the sale of goods and the provision of services.

- Under a sale contract, the seller undertakes to deliver specified goods to the buyer, against the payment of a set price. The sale transfers the ownership over the goods to the buyer, together with the related warranties.<sup>15</sup> Depending on the particular transaction considered,

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<sup>13</sup> As it will be evidenced in the following section, most special legislations do not deal with the contract type applicable to the particular contract or obligation.

<sup>14</sup> Some legislations cover only a specific sector or commodity, see *infra* Cataluña law dealing with husbandry contracts, or in the US, the Wisconsin "Vegetable Procurement Practices".

<sup>15</sup> Other contract types may involve an actual transfer of ownership: for example in Brazil, the "*contrato de mútuo*" is a common contractual structure for hog production contracts. See Coser, F.J., *Contrato de integração de suínos: formatos, conteúdos e deficiências da estrutura de governança*



the producer could be either the seller delivering the production to the contractor, or the buyer of inputs – animals, seeds or plants – from the contractor. Parties would enjoy a certain flexibility to adapt their obligations (for example to agree on a series of elements such as when title passes together with the risks). However, certain aspects often present in the context of an agricultural production relationship may be critical in defining the legal regime as a sale: it could be so when specifications would not only concern the final product but would deal with processes and techniques involved,<sup>16</sup> possibly entailing a characterisation as a contract for services involving the supply of materials rather than a sale of goods.

- Under a contract for services, the producer undertakes to provide his labour and skills against a price set according to the results of his activity. The contractor would provide the raw materials and will retain ownership through the production process. Under the contract also the contractor will be called to undertake services whether directly in relation to the soil or goods, or in providing directions or advice for the producer to follow in the performance of his obligations.

Depending on the legal system, other legal categories (often based on traditional agrarian or land law concepts) may be used by the parties or may become relevant to characterise their obligations:<sup>17</sup>

- In many countries, especially regarding livestock, a variety of local forms may apply falling under a general concept of lease, loan or other forms.<sup>18</sup> Under agreements falling under this broad category, the farmer would be granted the use of the animals owned or managed by the contractor for a period of time, and over this period, the farmer would be responsible for the condition of the property.
- In some common law jurisdictions, bailment – whereby farmer is entrusted with the possession of the contractor's property and must take care of the goods – provide the contractor with extended protections over the use, sale or other kinds of transfer of seeds or crops of special brands or genetically modified produce when the contractor holds intellectual proprietary rights.<sup>19</sup>
- In a number of Latin American countries, under a "maquila" contract the producer undertakes to supply raw material to a food manufacturer or agribusiness and the latter undertakes to

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*predominante na suinocultura brasileira*, Dissertação de mestrado em agronegócios Universidade de Brasília, Faculdade de agronomia e medicina veterinária (2010).

<sup>16</sup> Drawing a distinction between a sale involving goods to be produced and a service contract is not easy, and will rely on domestic legal definitions and judicial interpretation. As an interesting reference in the context of the United Nations Convention on contracts for the international sale of goods, ref. Article 3 and CISG-AC Opinion no 4, *Contracts for the Sale of Goods to Be Manufactured or Produced and Mixed Contracts (Article 3 CISG)*, 24 October 2004. Rapporteur: Professor Pilar Perales Viscasillas, Universidad Carlos III de Madrid: "The criteria to be followed include, among others, the comparison between the obligation to do and the obligation to give; the character of the object/goods (fungible/nonfungible; standard/custom-made); the possible alteration of the object (whether or not an item with its own individuality is created); whether the production of the goods was done before the contract, or if the goods belong to the kind of goods that are usually produced by the seller; the skill of the person who is to produce the goods; and, finally, the need to transfer property in the goods"

<sup>17</sup> The legal forms indicated are mere examples of the variety of structures that may be part of agricultural production contracts. Further study will be needed to identify more precisely what forms can be involved (or typologies of forms) and the implications over the parties obligations.

<sup>18</sup> For example in France the "*bail à cheptel*" under Code civil art. 1800 or husbandry leases regulated by *Code rural* art. L. 411-1; in Brazil, as an example of loan, the "*contrato de comodato*" is also commonly used for animal production contracts. See Coser *supra* note 15.

<sup>19</sup> For a description of bailment as a legal form specified in grain production contracts in the US, in particular for seed production, cf. Hamilton, *Farmer's Legal Guide ... supra* note 8, at pp. 36 and 49.

process the produce. During processing, the contractor acts as the depositary of the product until it is delivered to the producer, and is entitled to a share of the final processed product.<sup>20</sup>

- Depending on the actual arrangements between the parties, or under the provisions of the law, the relationship may be in the nature of a collaboration with both parties contributing to a common venture, sharing risks and profits.<sup>21</sup> As a rule, arrangements of this kind would not *per se* create a separate legal entity. However, should it be considered as a joint venture or a partnership, potential implications may derive regarding the financial liabilities of the parties for example in the event of insolvency.

29. Land tenure issues may be involved in agricultural production contracts. Depending on the particular arrangement, a private company with title over the land may lease land to farmers for contract farming, a situation which is likely to be found in developing countries where traditional landowners or large investors would deal with small scale farmers with no formal tenure rights.<sup>22</sup> Under other situations, the company may lease the land from landholders, with shared responsibilities in the production and the benefits. Or, under a particular form of production contract, contractor may contribute land and producer may contribute other assets and labour.<sup>23</sup>

30. Although an agreement is designated as a “production contract” issues may indeed arise regarding its legal nature when contractor provides a large range of services regarding the management of the farm, and could be considered rather as a tenant of the owner of the land.<sup>24</sup>

31. For agribusiness companies, dealing on the basis of a contract is generally seen as providing an alternative to being involved in land issues under direct investment transactions. Also for producers, specific benefits are to be derived from non equity forms of investment. The question whether contracts covering both land tenure and production aspects should be contemplated in the future Guide will have to be considered.

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<sup>20</sup> This contract is regulated *e.g.* under Argentina law No. 25113 of 23 June 1999 (*contrato de maquila o depósito de maquila*) which applies to contracts for the supply of agricultural and husbandry raw material for its processing, manufacturing and/or transformation (Art. 4). During processing, the contractor acts as the depositary of the product until it is delivered to the producer, and is remunerated for the service provided by a percentage of the transformed produce or its equivalent in cash. See also Art. 134 of the Panama Agrarian Code on the “agribusiness contract” *infra*.

<sup>21</sup> Partnership could derive *e.g.* under the *maquila* contract under Argentina law, and under the integration contract regulated by Cataluña law; see also the Brazilian bill specifying in art. 3: “The integration relationship is characterised by the joint use of resources and efforts and joint distribution of results. This is a leading principle upon which this law is to be applied and interpreted.” It is worth noting that the future legislation aims at providing a new legal form after law 11.443 of 2007 expressly declared that the “*contrato de parceria*” could no longer apply to agro-industrial contracts.

<sup>22</sup> Eaton, C. and Shepherd, A., *supra* note 5, p. 65 classify contracts including land tenure specifications as an extension of the “management and income specification contract”: they are described as being entered into by private corporate sector or national development agencies; they contain clauses relating to land tenure and land use conditions, normally involve directed contract farming with high degree of material and management inputs, and are common under centralised and nucleus estate models.

<sup>23</sup> See Cataluña law art. 6(2). The integration contract does not lose its characterisation if contractor supplies grazing land, provided that producer supplies fixed facilities.”

<sup>24</sup> It may be noted in this context that in the United Kingdom, “contract farming” is used as a loose term to apply to a variety of arrangements whereby a farmer (landowner or tenant) farms land with contractors. The farmer keeps full control of the land and of the output, makes all key decisions about cropping and strategy and instructs contractors to provide services which range from individual operations to more comprehensive packages of services (labour, machinery and some day-to-day management, *e.g.* crop management).

32. While the legal types referred to above can be used, also in a combined form, to structure an agricultural production contract, this could not be so regarding the employment relationship, which is subject to special public policy regulations. When the farmer's independent legal capacity is not clearly evidenced (for example on the basis of a formal registered agricultural enterprise or a defined business status) the possible characterisation as an employment would rely on criteria related to the level of farmer's autonomy to make decisions and manage the enterprise, the scope of the actual authority and control of the integrator over the producer. As an employee, the farmer should be entitled to the legal provisions and protection of the labour and social regulation applicable such as minimum wages, sick leave and other social benefits. On the other hand, he would lose all the rights attached to his quality of agriculture enterprise (fiscal regime, land rights, public subsidies etc.).

33. Agricultural production contracts involve a number of features that are typical of well-known specific types of contracts. For those features, existing rules and practices relating to those specific contracts may be relevant for formulating guidance on agricultural production contracts.

### C – Specific legislation regulating agricultural production contracts

34. A number of countries have enacted (or are preparing) special legislative acts to deal with agricultural production contracts, defining a special type of contract subject to special rules.<sup>25</sup> While not exhaustive, the following list contains representative examples of such legislation for the purposes of the present document.

**France** – Integration contract ("*contrat d'intégration*") regulated by law n° 64-678 of 6 July 1964 and amended by law n° 80-502 of 5 July 1980 - reproduced in art. L. 326 et seq. of the *Code rural*), and implementation rules for standard agreements regulated by provisions R326-1 to R326-10 of the *Code rural*;

In **India**, the *Agricultural Produce Marketing Act* (APMC) was developed in 2003 at federal level as a model act to assist the states in removing barriers which introduced inefficiencies and monopoly rents in the functioning of agricultural markets. It includes a Chapter on contract farming agreement, together with a Model Agreement for Contract Farming, which is subject to extensive explanatory notes contained in an Addendum to the Model Act. States are in the process of implementing state legislation and model contracts.

In **Morocco**, law n° 04-12 on agricultural aggregation ("*loi n° 04-12 relative à l'agrégation agricole*" promulguée par Dahir n° 1-12-15 du 17 juillet 2012) (adopted together with a law the agricultural and fishery interbranch organizations – "*loi n° 03-12 relative aux interprofessions agricoles et halieutiques*") is part of a State lead modernization programme of agriculture, *Plan Maroc Vert* ([http://www.ada.gov.ma/Plan\\_Maroc\\_Vert/plan-maroc-vert.php](http://www.ada.gov.ma/Plan_Maroc_Vert/plan-maroc-vert.php)), in the form of a public-private partnership, whereby both parties to "integration projects" submitted by the private sector and approved by the public competent authority are eligible to public financial support.

In **Panama**, law 55 of 23 May 2011 introduced a new Agrarian Code, Part IV of which deals with "Vertical Integration in Agriculture and Agribusiness relationships" with Chapters on the "agribusiness contract" and on the "agrimarketing contract". General provisions applicable to the various contracts regulated are also contained in the Code (Arts. 41-49)

[http://www.gacetaoficial.gob.pa/pdfTemp/26795\\_A/GacetaNo\\_26795a\\_20110530.pdf](http://www.gacetaoficial.gob.pa/pdfTemp/26795_A/GacetaNo_26795a_20110530.pdf)

In **Spain**, the Autonomous Community of Cataluña adopted law 2/2005 on integration contracts ("*contratos de integración*") dealing with husbandry contracts (<http://www.boe.es/boe/dias/2005/04/29/pdfs/A14615-14618.pdf>) and implementation rules with a

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<sup>25</sup> Similarities may be found with the special protections afforded under consumer law, insurance law, or franchise law.

model contract form (*Resolución ARP/2974/2005 of 13 de octubre, por la que se aprueba el modelo homologado de contrato de integración*) [http://www.porcat.org/download/resolucion\\_arp\\_2974\\_2005.pdf](http://www.porcat.org/download/resolucion_arp_2974_2005.pdf)

In the **USA** at federal level, different acts may be relevant to parties' obligations under a production contract, such as *The Packers and Stockyards Act 1921* and *The Perishable Agricultural Commodities Act (PACA)*. Several states have adopted specific legislation or provisions on production contracts (the first was Minnesota in 1990 with subsequent amendments) and a *Model Producer Protection Act (MPPA)* was drafted in 2000 ([http://www.state.ia.us/government/ag/latest/news/releases/producer\\_act.html](http://www.state.ia.us/government/ag/latest/news/releases/producer_act.html)) upon which several states (Arkansas, Georgia, Illinois, Iowa, Kansas, Wisconsin) have based their legislation (some of which only for a specific sector in particular livestock and/or poultry, or swine – or vegetables production).<sup>26</sup> The following acts provide examples of such regulations:

– **Iowa** Producer Protection Act (2000)

[http://www.state.ia.us/government/ag/working\\_for\\_farmers/2000\\_news/producer\\_protection\\_act.html](http://www.state.ia.us/government/ag/working_for_farmers/2000_news/producer_protection_act.html)

– **Minnesota** Agricultural Contracts Act: <https://www.revisor.mn.gov/statutes/?id=17>

– **Illinois** Agricultural Production Contract Code (2010 Illinois Code Chapter 505 Agriculture 505 ILCS 17 <http://law.justia.com/codes/illinois/2010/chapter505/2485.html>)

– **Wisconsin** “Vegetable Procurement Practices” (Agriculture, Trade & Consumer Protection (ATCP) 101.01, Wisconsin Administrative Code (2011)

[http://docs.legis.wisconsin.gov/code/admin\\_code/atcp/101.pdf](http://docs.legis.wisconsin.gov/code/admin_code/atcp/101.pdf)

In **Vietnam** Decision no. 80/2002/qd-ttg of June 24, 2002 on Policies to Encourage the Contractual Sale of Commodity Farm Produce sets out a number of key policies to encourage enterprises to sign farm “production-sale” contracts with producers and deals with the responsibilities of the concerned ministries, branches and organizations and regulates in detail the terms of the contract, non performance and remedies issues <http://policy.mofcom.gov.cn/english/flaw!fetcandh.action?libcode=flaw&id=d2e55c69-9b57-4bfb-af4d-02171f7e121f>

and Guidance on the form of contracts on Sale of commodity farm produce (farming contract) in accordance with Decision 80/2002/qd-ttg (77/2002/QĐ-BNN) (English translation not found)

In **Brazil**, the Senate is examining a bill relating to contracts of partnership for the integrated production of agricultural products (*contratos de parceria de produção integrada agropecuária*)

[http://www.senado.gov.br/atividade/materia/detalhes.asp?p\\_cod\\_mate=100728](http://www.senado.gov.br/atividade/materia/detalhes.asp?p_cod_mate=100728)

35. The listed legislative and regulatory acts apply to contracts concluded by producers to organise the production and delivering it to the contractor. Their common purpose (sometimes stated in a preamble or annotations) is to promote security in contracts and help parties to deal on a more equitable basis. The provisions considered relate to the private relationships between the parties and they are often included as part of a broader programme to promote and modernise the agricultural sector and to organise a more efficient coordination with the market, with accompanying legislation to strengthen producer organisations as well as other public policy measures, in particular the provision of financing to eligible parties.

36. As a consequence, most acts refer specifically to contracts linking producers to the food industrial and commercial sector or companies; some apply exclusively to such relations. Also, certain acts apply to one particular kind of commodity, typically husbandry or vegetables.

37. Regarding the contractual type defined under the various legislations, it is possible to find the following common features:

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<sup>26</sup> See Peck, A., “State Regulation of Production Contracts”, May 2006, A National Agricultural Law Center Research Publication.

– both parties undertake to supply goods and/or services to each other, thus being bound by “reciprocal obligations”.<sup>27</sup> It is sometimes expressly specified that this test would not be satisfied when one party’s obligation were limited to paying a price.<sup>28</sup>

– contractor has a leading role in organising / managing the production: this is either expressly stated <sup>29</sup> or can be inferred from the provisions of the act relating to the obligations of the parties. Under French law, one essential feature of the “integration contract” is that the producer is subject to the contractor’s economic decisional power, evidencing the producer’s “economic dependency” on the contractor.<sup>30</sup>

38. Under the special legal regime created under the cited legislations, certain mandatory rules would apply. <sup>31</sup> A common approach is to ensure a procedural protection to the producer by setting minimum requirements regarding the form of the contract. In all cases contracts must be in writing and contain designated information, referred to either generically or in a detailed form. This is required to strengthen the position of the producer at the time of the conclusion of the agreement by ensuring transparency and clarity regarding the content of the undertaken obligations. The information would enable the producer to be aware of the benefits to be expected but also of the potential risks incurred. <sup>32</sup>

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<sup>27</sup> France, Art. 326-1(1). The reciprocal obligation may be performed under several separate but joined agreements entered into by producer with several industrial or commercial companies (art. 326-1(2)). This provision has been specified in caselaw by requiring that the various contracts be “entered into each in the perspective of the other(s)”, a criterion which evidences a group of contracts based on linked transactions and a coordinated commercial policy.

<sup>28</sup> France (Art. 326-3); Brazil Art. IV.

<sup>29</sup> See for example under Illinois law, production contract is defined as “[any] document [...] under which provisions (i) the producer would sell to a contractor [...] ; and (ii) the contractor has, or exercises some control or direction over, the production process; [...]. [...] control or direction over the production process includes: (i) the contractor’s designation of special commodity characteristics, such as those present in value-enhanced grains or specific genetics in livestock; or (ii) the contractor’s designation of a production input, such as seed variety, to be used by the producer to fulfill the production contract.”

See also *e.g.* Cataluña law, Art. 9 referring to the “integrator’s obligations” at (g): “to undertake the direction and technical management of the farm”.

In the USA, an authoritative definition of “Production contract” is proposed by Hamilton, *Farmer’s Legal Guide ... supra* note 8, p.1: “An agricultural production contract is a legally binding agreement of a fixed term, entered before production begins, under which a producer either: agrees to sell or deliver all of a specifically designated crop raised on identified acres in a manner set in the agreement to the contractor, and is paid according to a price or payment method, and at a time, determined in advance; or agrees to feed and care for livestock or poultry owned by the contractor until such time as the animals are removed, in exchange for a payment based on the performance of the animals.”

<sup>30</sup> Based on the definition under Art. 326 - Art. 326-3, French courts have characterised a contract as an “integration contract” when producer and contractor perform a *plurality of obligations* which may take a variety of forms but evidence the producer’s “economic dependency” on the contractor. This has been the case for example, when the parties have agreed on exclusivity arrangements (for the supply of inputs or for the marketing of the produce) or financing arrangements implying production quotas. When both parties perform reciprocal obligations but when there is no evidence of subordination, the contract would be a simple supply contract and the law on integration contract would not be applicable.

<sup>31</sup> This section will be expanded with specific references provided in Part II of this document under the corresponding chapters dealing with the content of the contract (Chapters I to X).

<sup>32</sup> An example of a strict procedural approach is provided by the Moroccan law.

39. Also, in view of the importance of providing certainty to the parties regarding the practical enforcement of their contractual and legal remedies, almost all cited legislation contains provisions dealing with alternative dispute resolution mechanisms, often arranging for special settlement bodies.

40. In addition to the requirements as to form, legislation may also contain provisions regulating the parties' substantive obligations. In particular, these provisions aim at restricting unfair practices and reinforcing producer's protection, by restating the application of concepts or principles included elsewhere in the law (under general contract law provisions or special pieces of legislation), or by providing for specific remedies for the producer.<sup>33</sup> While most legislations leave the parties with an ample freedom to regulate their relationship, another approach would impose a balance of rights and liabilities upon the parties.<sup>34</sup>

41. In an effort to promote the use of a fairer and balanced regulation of the contractual relationship, some legislations expressly refer to and regulate collective contracts that can be negotiated at inter-branch level to apply to a particular commodity or in one particular commodity sector, and for a specified agricultural period.<sup>35</sup> Agreements concluded by participants in accordance to the legal specifications and approved by a public authority may be mandatory for all private contracts entered into in the corresponding sector. Another way to introduce a control over parties' autonomy is to develop model contract forms which are annexed to the special legislation, either for individual or collective contracting, providing more detailed content and guidance to parties; such model forms and may be likewise be subject to public authority's approval.

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<sup>33</sup> Certain US states act, for example Iowa, provide examples of legislation providing rather extended substantive protections to producer.

<sup>34</sup> See Cataluña law, arts. 1 and 2, providing that the "integration" form regulated is based on a "collaboration" where the parties' entitlement to profits is based upon their contributions and the production obtained; See also Brazil bill referring to a "partnership".

<sup>35</sup> See French law, Art 326-5;

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## Introduction \*

1. The introduction to the future Guide should present the notion of contract farming, outline its economic and social benefits and risks, describe the various modalities and types of contract farming used in practice, present the various approaches taken by domestic regulations, define the type of contract farming that the future Guide should treat and explain the approach taken in the future Guide to legislative and contractual issues.

## Chapter I – Parties to the agricultural production contract

2. It is proposed that this chapter should describe the parties that are typically bound by an agricultural production contract. They are essentially an agricultural producer and a contractor. Parties are generally referred to under special legislations as part of the definition of the contract regulated.

3. In countries where certain commodities are part of regulated markets and could not be traded directly between the parties, a special rule in contract farming legislation specifically allows direct contracting between producers and processors/manufacturers.<sup>1</sup>

### A – The agricultural producer

4. This section should discuss the extent to which general provisions of the applicable law relating to the form of agricultural enterprises, to legal status and capacity of agricultural producers, and to commercial activities are relevant.

5. Parties would generally refer in the contract to a specific designation referring to “grower”, “elevator”, “farmer” etc. and a designated commodity (some legislative definitions describe a specific area or activity<sup>2</sup> or refer to a broad legal concept of “agriculture”, “agricultural activity” or “agricultural producer” defined under a separate body of legislation).

6. Individual producers must have an independent legal status. This section should present the broad range of natural and legal entities that could be involved based on the available legal

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\* This document proposes a tentative outline of the future Guide with a view to eliciting comments and discussions within the Working Group. In some cases, this has been done by a non exhaustive listing of issues proposed for discussion in the future Guide, while other parts include annotations. The acts and legislations reported are not intended to provide a comprehensive review of existing legislations and additional study will be needed to fully analyse their provisions.

This document is to be completed by additional documents referring to specific issues in relation to agricultural production contracts.

<sup>1</sup> See India Model Act on Agricultural Marketing.

<sup>2</sup> Under US acts relating to production contracts, “contract producer” would be defined in relation to the particular activity: see for example under Iowa Act, ““Contract producer” means a producer who holds a legal interest in a contract operation and who produces a commodity under a production contract”; ““Commodity” means livestock, raw milk, or a crop” while each of these concepts is likewise defined under the law. Under French law an “agricultural producer” for the purposes of an “integration contract” will derive from the definition of “agricultural” activities (art. L 311-1 *Code rural*) as “all activities involving control and operation of a vegetal or animal biological cycle which form one or several phases necessary to the completion of the cycle, as well as the activities carried out by an agricultural operator which are in furtherance of the production action or which are performed on the farm. The agricultural activities so defined have a civil nature”).



categories under domestic law.<sup>3</sup> Special attention should be given to producer organisations and cooperatives.

7. In certain jurisdictions, “civil” as opposed to “commercial” status of the farmer or its capacity as a “merchant” may be relevant regarding the characterisation of the contract and with resulting consequences on the applicable rules (on for example enforcement, standards applied in performance, etc.).<sup>4</sup>

8. This section should further consider the effect of requirements that the producer under an agricultural production contract be registered/licensed with a prescribed authority.<sup>5</sup>

9. This section should further discuss the importance of evidence of an independent legal status for the enforcement of the agreement as an agricultural production contract. Indeed, under certain circumstances, a producer lacking independent legal status may be found to act as an employee or agent of the contractor with the risk of the contract being declared void and the relationship being re-characterised by the court no matter the designation given by the parties. Contracts of agricultural production and employment contracts are incompatible legal categories.<sup>6</sup> This can have a particular importance when the contract is entered into with farmers in the informal sector.

10. Another important distinction to be drawn in this section is between an agricultural production contract and a tenancy contract. In this context, producer must be able to show that it is actively in business and takes risks pertaining to its activity.

## **B – The contractor**

11. This section should describe the typical nature and organisation of the contractor. In most cases, the contractor will be a commercial entity engaged in food processing and marketing activities<sup>7</sup> and subject to domestic company law regulations. Special requirements generally apply that the contractor be registered / licensed with a prescribed authority.<sup>8</sup> (intended *inter alia* to provide information regarding financial credentials).

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<sup>3</sup> See Under Moroccan law: “any agricultural producer, natural or legal person subject to public or private law, including cooperatives, associations and Economic Interest Groupings gathered by the integrator with a view to implementing an agricultural aggregation project”; under the Model contract farming agreement annexed to the Indian Model Act (I-b), “Contract Farming Producer/s includes an agriculturist, farmers’ associations, self-help groups, authorised tenants and farmers cooperatives societies registered under the State Cooperative Act.”

<sup>4</sup> For a discussion of the implications of the producer being or not a “merchant” in the US context, see Hamilton, *Farmer’s Legal Guide ... supra* note 8, pp. 24-25; The type of contract contemplated under Cataluña law is stated to be of a “civil” nature (Art. 2).

<sup>5</sup> India Model Act, art 38(1). Vietnamese law: Moroccan law: Arts. 4-6

<sup>6</sup> This is spelled out in Cataluña law, Art.2(4). In France, see Cons. d’Etat 2 juillet 1982, Dr. fiscal. 1983, 501, concl. Rivière. Similarly in the US, see the Oklahoma Attorney General Opinion dated April 11, 2001 reported by Miller, J.A., “Contracting in Agriculture: Potential Problems”, 8 *Drake Journal of Agricultural Law* (2003), p 67. For examples of clauses see *idem*, pp. 65-68. Miller also discusses the possible implication over small producers of including the “independent contractor” requirement in the law.

<sup>7</sup> See e.g. Minnesota Act : ““Contractor” means a person who in the ordinary course of business buys agricultural commodities [...]or who contracts with a producer to grow or raise agricultural commodities [...]” Under French law, under an “integration contract” the contractor must be incorporated as “an industrial or commercial company” (Art. 326-1(1)); Panama law (art. 134) refers to an agreement involving “an agribusiness party”; when contractor does not meet this requirement, the relationship will be subject to a different legal regime.

<sup>8</sup> Cf. *supra* note 4.

12. Contractor may be an affiliate or subsidiary of another entity. The extent to which contractor is legally independent from the other entity, and whether the other entity might be held liable for contractor's default under the contract should be discussed.

13. This situation is likely to occur when a transnational corporation based in a foreign country is involved. The corporation would typically operate locally through a local contractor, generally an independent legal entity, incorporated and operating under the law of the country of production. A main contract will be concluded by the foreign company with a local entity, while the latter would subcontract to producers in accordance with the specifications of the main contract. The relationships between the main company and the local contractor and their potential implications regarding the contract and related issues should be considered.

14. The contractor may also be another private, non commercial, entity.<sup>9</sup> This would be the case for example when the contract involves another agricultural producer (or group of producers) which does not have a "commercial" status or is not a "merchant" under the applicable law.

15. Other categories than commercial entities are sometimes contemplated as a party to an agricultural production contract. These include in particular:

- public entities: government or other public sector legal entity (possibly leading to the application of special rules dealing with public procurement contracts)
- cooperatives for relationships with members (based on a contractual relation or otherwise): certain legislations on agricultural production contracts expressly provide that they do not apply to such relationships<sup>10</sup>, while others do apply to such relationships<sup>11</sup>
- contractor may contract with producer through an intermediary.

### **C – Other parties**

16. This section should refer to other parties that may to a lesser or greater extent intervene in the contract or support its negotiation, operation and performance.

#### **C1 – Other parties to a single contract**

17. Third parties may participate in the overall transaction under different capacities:

- a public entity for example under a public private partnership project<sup>12</sup> as a facilitator or as a finance provider;

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<sup>9</sup> Under Moroccan law, an "aggregator" is defined as "any natural or legal person subject to public or private law, including cooperatives, associations and Economic Interest Groupings gathering aggregated parties with a view to implementing an agricultural aggregation project"; also under the Model contract farming agreement annexed to the Indian Model Act (I-a), a "contract Farming Sponsor" may be "a sole proprietor, a company registered under the Companies Act, 1956, a partnership firm registered under the Partnership firm 1932, a Government Agency, a Cooperative Societies registered under the State Cooperative Societies Act [...]"; under Cataluña law, no requirement is included regarding the commercial capacity of contractor.

<sup>10</sup> Under Section 19.9442, Minnesota Act provisions regarding contract requirements do not apply to agricultural marketing contracts between a capital stock cooperative and its members; the Brazilian bill likewise excludes cooperative relationships. Under French legislation, art. 326-5: internal relations between the cooperative and its members do not qualify as integration contracts, but the cooperative may enter into such contracts with non members.

<sup>11</sup> See *supra* note 9.

- third party creditors, such as the landowner or a financial institution providing credit to farmer, (with contractor's agreement to repay the loan directly with deduction from payments to producers)
- other participants may include:
  - non-governmental organisations (NGO): as a facilitator, as a finance provider
  - third party guarantors <sup>13</sup>
  - certification agents

## **C2 – Relationships involving several contracts**

18. This section should examine complex integrated production relationships involving several contracts with different functions and parties:

- such situations are contemplated in certain special legislations: *e.g.* in the US (*inter alia* Iowa), two different contractors may be involved: an "active contractor" who owns the commodity, and a "passive contractor" who furnishes management services. The production contract may be concluded between producer and both contractors, or with the passive contractor only, provided the passive contractor has a contractual relationship with the active contractor involving the production of the commodity. <sup>14</sup>
- see also under French law, "integration contract" is defined as "an agreement *or several separate agreements* between an agriculture producer or group of producers *and one or several* industrial or commercial companies". The integration relationship may involve several contracts with different functions and parties but which are linked together. <sup>15</sup>

## **Chapter II – Contract formation and contract form**

19. This section should discuss the contractual practice regarding negotiation and conclusion of agricultural production contracts and the application of rules contained in national law relating to formation of contracts.

20. In the context of contract formation, defects regarding the consent of the parties at the time of contracting should be considered. Matters such as capacity to contract, mistake, error, threat, fraud and gross disparity in contract terms will be governed by mandatory provisions of domestic law, and may entail the illegality of the contract. For the purposes of this document, clauses affording a highly imbalanced advantage to contractor and contractor's actions tending to exercise a undue influence on producer or amounting to an "unfair practice" will be discussed under Chapter IV on Contract terms and contractual practices.

21. Legislations which introduce a special regime for agricultural protection contracts all base the protection afforded to producer on the written form and minimum content requirements of the contract. This is to provide transparency and certainty regarding the obligations undertaken by the parties and their possible implications.

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<sup>12</sup> This is the general context in which individual contracts between producers and contractor would be concluded under "aggregation projects" regulated by Moroccan law.

<sup>13</sup> Under most US state laws, if a contractor is required to obtain a license to purchase agricultural commodities, the licensing authority may require the parent company of a licensee subsidiary to guarantee payment or contract performance as a condition of licensing See *e.g.* Minnesota Act section 17.93.

<sup>14</sup> Iowa Act, Section 2.

<sup>15</sup> French law, art. 326-1(2). This concept has been specified in caselaw by requiring that the various contracts be "entered into each in the perspective of the other(s)", a criterion which evidences a group of contracts based on linked transactions and a coordinated commercial policy.

- The written document is intended to provide to producer an advance information regarding the terms of the contract. It may be in the form of a pre-contractual document.<sup>16</sup>
- US production contract legislations grant producers the right to cancel the contract within three days after its conclusion, or such other period as designated by the contract.<sup>17</sup>

### **A – Requirements regarding written form**

22. Agricultural production contract practice reports frequent abuses deriving not only from agreements concluded orally but also from incomplete, poorly drafted, not readable written documents. Particular specifications may apply regarding how “written” form should be.

23. This section should discuss the function of “writing” requirement. This applies also to all contractual terms and conditions, and any change subsequently introduced.

24. Certain special legislations provide extensive details regarding a particular format of the document, “readability” or “legibility” requirements, kind of language to be used so as to be “understandable”, and particular specifications to better inform or alert the producer.<sup>18</sup>

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<sup>16</sup> Brazilian bill provides that agro-industrial company is under a duty to prepare and update every three months a “pre-contractual information document” to be submitted to the prospective producer, which must report detailed technical and financial information, as well as the parties obligations and allocation of liabilities.

<sup>17</sup> See: US Producer Protection Act: Section 5; Minnesota Act section 17.941.

<sup>18</sup> US state legislations provide a particularly illustrative example. The relevant provisions of Minnesota Act are reproduced hereunder :

17.942 Cover Sheet Requirements - Subdivision 1.Mandatory cover page. An agricultural contract [...] must contain as the first page, or first page of text if it is preceded by a title page or pages, a cover sheet as provided in this section. - Subd. 2.Requirements. The cover sheet or sheets must comply with section 17.943, and must contain the following: (1) a brief statement that the document is a legal contract between the contractor and the producer; (2) the statement “READ YOUR CONTRACT CAREFULLY. This cover sheet provides only a brief summary of your contract. This is not the contract and only the terms of the actual contract are legally binding. The contract itself sets forth, in detail, the rights and obligations of both you and the contractor. IT IS THEREFORE IMPORTANT THAT YOU READ YOUR CONTRACT CAREFULLY.”; (3) the written disclosure of material risks required by section 17.91, subdivision 2; (4) a statement detailing, in plain language, the producer's right to review the contract as described in section 17.941; and (5) an index of the major provisions of the contract and the pages on which they are found, including: (i) the names of all parties to the contract; (ii) the definition sections of the contract; (iii) the provisions governing cancellation, renewal, or amendment of the contract by either party; (iv) the duties or obligations of each party; and (v) any provisions subject to change in the contract.

17.943 contract format. Subd. 1.Readability. An agricultural contract must be in legible type, appropriately divided and captioned by its various sections, and written in clear and coherent language using words and grammar that are understandable by a person of average intelligence, education, and experience within the industry. Subd. 2. Exceptions. Subdivision 1 does not apply to particular words, phrases, provisions, or forms of agreement specifically required, recommended, or endorsed by a state or federal statute, rule, or regulation. Subd. 3.Customarily used terms. An agricultural contract may include technical terms to describe the services or property which are the subject of the contract, if the terms are customarily used by producers in the ordinary course of business in connection with the services or property being described.

See Also Brazilian bill, Art. 4.

## B – Requirements regarding contract content

25. This section should discuss the implications of statutory requirements of a minimum content or certain specific terms to be mandatorily included in a production contract, in the interest of transparency and full information of producer.

26. Terms may be listed in a more a less detailed form. They usually include:

- parties identification
- designation of the land or livestock subject to the contract, and facilities provided
- product specifications for delivery (such as quantity/yield and quality of product, place and time of delivery)
- inputs and services to be supplied by the contractor, including level of intervention as regards production management
- price determination and payment conditions
- duration, renewal, termination, amendment and renegotiation of contract; <sup>19</sup>
- compensation payable for production loss, or contract non compliance due to force majeure causes, damages for breach; <sup>20</sup> etc.
- responsibility for obtaining and complying with public permits; <sup>21</sup>
- allocation of responsibilities for waste disposal, improper use of inputs and for possible environmental damage ...

27. Disclosure requirements serve to provide producer with clear information of the implications of entering into the contract. Several legislations require specifically the contract to inform the producer of the “risks involved” <sup>22</sup> on the basis of detailed elements to be taken into consideration. In this context, reference is made to a “check list” <sup>23</sup> or a model contract form annexed to the law <sup>24</sup> to be negotiated with producer organisations. One crucial element refers to the amount of investment

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<sup>19</sup> France Art. 326-6; Morocco law art. 9.

<sup>20</sup> See Cataluña law, Ar. 6

<sup>21</sup> See the US Producer Protection Act 2000, Section 4a – also *e.g.* in Minnesota Act section 17.91(2).

<sup>22</sup> *E.g.* the US Producer Protection Act 2000, Section 4a.; Minnesota Act. 17.91(2): “An agricultural contract must be accompanied by a clear written disclosure setting forth the nature of the material risks faced by the producer if the producer enters into the contract. The statement must meet the plain language requirements of section 17.943. The statement may be in the form of a written statement or checklist and may be developed in cooperation with producers or producer organisations.”; see the information to be reported in the “pre-contractual information document” under Art. 8 of the Brazilian bill, including *inter alia* (iii) information regarding “health and environmental requirements and economic risks inherent to the activity”;

Requirement of information regarding the risks involved may derive from judicial interpretation. In France, see Art. 326-6 requiring the contract to set the nature, price and quality of the reciprocal obligations of the parties; courts apply a strict standard in requiring that the clauses be sufficiently detailed so as to enable the producer “to obtain an accurate assessment of the performances that he will receive in exchange for his obligations” or to “determine the likely return of his activity”.

<sup>23</sup> See US Producer Protection Act 2000, Section 4b See Minnesota Act, section 17.942 subd 1 and 2

<sup>24</sup> See *e.g.* France implementation regulations art. R326-1 to R326-10. Also Cataluña law implemented with a model contract form (Resolución ARP/2974/2005).

required on the producer's side over the life of the contract.<sup>25</sup> Other elements would involve the disclosure of contractor's financial and business standing<sup>26</sup>

28. The legislation may also require the contract to spell out the rights that the producer is granted under the law itself.<sup>27</sup>

### **C – Contract documents**

29. The contract may be formed of one main document as well as other negotiated or standard documents, for example specifying technical rules or referring to regulations (such as public requirements regarding quality standards) or other provisions (such as a standard terms) which are incorporated by reference and apply to one or another specific aspect of the relationship.

30. Standard forms of contract ("adhesion contracts") are frequently applied by large contractors in their dealings with a large number of individual producers are often subject to specific requirements under special legislations and most often under general contract law.

31. On the other hand collective agreements negotiated with producer organisations provide added security, while a large number of producers linked to a single contractor may lead to a fragmentation and disparity of treatment: this situation is dealt with under one legislation on production contract.<sup>28</sup>

### **D – Contract disclosure and review**

32. Most legislations on agricultural production contracts set rules on disclosure and submission of contract to a public authority:

- US production contract legislations prohibit confidentiality clauses which purport to prevent producers to disclose the content of the contract with third parties.<sup>29</sup>
- Also, such legislations provide for the review of contract by a public authority to ascertain its conformity to requirements as to form.<sup>30</sup>

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<sup>25</sup> Under Moroccan law Art. 10, the integration contract must also report information regarding the various arrangements under the whole integration project, in particular as regards financing, investment, supply of inputs, insurance arrangements.

<sup>26</sup> Under Morocco law, before being implemented, an aggregation project must be approved by the competent authority, and a certificate is released to both parties to the aggregation contract (Arts 4 and 5).

<sup>27</sup> For example under Section 5 of US Producer Protection Act 2000, stating producer's right to cancel the contract within three day of its conclusion also provides that "The contract producer's right to cancel, the method by which the contract producer may cancel, and the deadline for canceling the production contract shall be clearly disclosed in every production contract".

<sup>28</sup> French law, Art. 326-4 provides that when the number of individual contracts between producers and one single industrial and commercial company is over a number fixed by the ministry of agriculture, or when at least two third of the total number of producers under a contract with a single company so request, the individual contracts will be replaced by a collective contract reflecting the standard agreement of the sector concerned.

<sup>29</sup> Confidential clauses are unenforceable under USA Farm Security and Rural Investment Act of 2002; under the Packers and Stockyards Act 2008 revision; the Model Producer Act, adopted in various forms by several states, voids confidentiality clauses. See *e.g.* Iowa Act, Section 6. For examples of such clauses see: Miller, *supra* note 6, pp. 63-64 also discussing the need to recognise legitimate interests in protecting certain proprietary property.

<sup>30</sup> See US Producer Protection Act 2000, Section 4c and seq, regarding form and effects of review by a public authority [Commissioner/Secretary/Attorney General]; See Minnesota Act, section 17.944: Subd. 2

- Other legislations provide for different types of procedures
    - registration <sup>31</sup>
    - certification <sup>32</sup>
    - filing (or publicity or approval modalities) of the contract with a public authority with the establishment of a special registry for production contracts <sup>33</sup>
33. This section should consider the purpose and effects <sup>34</sup> of such requirements and consider which party should be under the duty to register.

#### **E – Consequences of defective contract formation and failure to comply with form requirements**

34. Defects regarding capacity and consent as well as non compliance with requirements regarding contract form will entail different consequences.
35. Under special legislations on agricultural production contracts, breach of contract form (contracts not in writing, missing clauses, insufficient readability) or contract content requirements (such as lack of adequate detail for the producer to assess risks), may result in:
- avoidance of the contract <sup>35 36</sup>

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“A contractor may submit an agricultural contract to the commissioner for review as to whether it complies with section 17.943.” Subd. 5 “A contract certified under subdivision 1 is deemed to comply with section 17.943. Certification of a contract under subdivision 1 does not constitute an approval of the contract’s legality or legal effect.”

<sup>31</sup> India Model Act: art 38(2) “The Contract Farming Sponsor shall get the contract farming agreement recorded with the officer prescribed in this behalf”.

<sup>32</sup> Vietnamese law, art. 4: “The commodity farm produce-sale contracts shall be certified by commune People’s Committees or authenticated by the district notary offices”.

<sup>33</sup> Cataluña law, Art. 5.

<sup>34</sup> Under France law, art. 326-5: Standard contracts are submitted to the ministry of agriculture for approval (“homologation”). One year after being approved, the standard agreement will apply to all agricultural producers and industrial and commercial companies of the sector concerned, and only those producers that will enter into contracts conforming with standard agreements will be entitled to receive financial subsidies.

<sup>35</sup> US state legislations see non compliance with form requirements as a major breach resulting in a variety of available remedies. For example, under see Minnesota Act, section 17.944 “Subd. 7. **Enforcement remedies.** A violation of section 17. 943 [referring to contract format requirements] is a violation subject to section 8.31, subdivision 1 [violations of the law respecting unfair, discriminatory, and other unlawful practices in business, commerce, or trade [...]]; Subd 8. **Reformation** “(a) In addition to the remedies provided in section 8.31, a court [...] may change the terms of the contract or limit a provision to avoid an unfair result if it finds that: (1) a material provision of the contract violates section 17.943; (2) the violation caused the producer to be substantially confused about any of the rights, obligations, or remedies of the contract; and (3) the violation has caused or is likely to cause financial detriment to the producer. (b) If the court reforms or limits a provision of a contract, the court shall also make orders necessary to avoid unjust enrichment. Bringing a claim for relief under this subdivision does not entitle a producer to withhold performance of an otherwise valid contractual obligation. No relief may be granted under this subdivision unless the claim is brought before the obligations of the contract have been fully performed.” Section 17.9441 sets **Limits on remedies.** In particular, Subd. 4 **Limits on producer actions.** Violation of section 17.943 [referring to contract format requirements] is not a defense to a claim arising from a producer’s breach of an agricultural contract. A producer may recover actual damages caused by a violation of section 17.943 only if the violation caused the producer to not understand the rights, obligations, or remedies of the contract. Subd. 5. **Statute of limitations.** A claim that an

- revision of the contract by the court <sup>35</sup>
- damages <sup>35</sup>
- penalties and sanctions including: civil penalties; criminal penalties;<sup>37</sup> cancellation of contractor's licence; <sup>38</sup> measures to affect contractor's reputation <sup>39</sup>

36. Defects regarding capacity and consent, such as mistake, error, threat, fraud and gross disparity will generally result in avoidance of the contract. This section should discuss under a general approach relevant aspects regarding avoidance based on agricultural production contract practice and legal applicable provisions. Aspects to be considered include:

- grounds of avoidance <sup>40</sup>

In this context, special grounds of avoidance afforded by legislations on agricultural production contracts should be considered: this applies in particular to producer's special protection under US state legislation: when producer has been required to make capital investment above a certain amount, contractor may be subject to restrictions on contract termination, avoidance, or failure to renew the contract. <sup>41</sup>

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agricultural contract violates section 17.943 must be raised within six years of the date the contract is executed by the producer.

<sup>36</sup> Cataluña law: Art 4(3): Oral contracts shall be void; See France Art. 326-6. Also when the prescribed clauses are not sufficiently detailed, the contract is voidable. Most recent caselaw has considered that this remedy being in the producer's interest, only the producer can claim it ("*nullité relative*" as opposed to "*nullité absolue*" when public policy is involved involving different time limits to bring the action under the rules of civil procedure). As a consequence, an integration contract has been considered legally formed although it had been concluded orally since the producer was not challenging its validity. See Also Brazilian bill, Art. 4, sanctioning violation of readability requirement with "partial or total" avoidance.

<sup>37</sup> Iowa Producer Protection Act, Section 13. Civil penalties may be due for unfair practice.

<sup>38</sup> Vietnamese law Article 5

<sup>39</sup> Vietnamese law Article 5: "The competent State bodies [...] announce on mass media the contractual breaches by the enterprises"

<sup>40</sup> See also para. 35 above and Chapter IV (including footnotes) on contract terms and contractual practices, where unfair terms and unfair practices may result in avoidance of the contract under the applicable law.

<sup>41</sup> See: US Producer Protection Act: Section 8. Production Contracts Involving Investment Requirements. And e.g. Minnesota Act Section 17.92: "**17.92 RECAPTURE OF CAPITAL INVESTMENT REQUIRED BY AN AGRICULTURAL CONTRACT.** Subdivision 1. **Notice and damages to be paid.** A contractor must not terminate or cancel a contract that requires a producer of agricultural commodities to make a capital investment in buildings or equipment that cost \$100,000 or more and have a useful life of five or more years until: (1) the producer has been given written notice of the intention to terminate or cancel the contract at least 180 days before the effective date of the termination or cancellation or as provided in subdivision 3; and (2) the producer has been reimbursed for damages incurred by an investment in buildings or equipment that was made for the purpose of meeting minimum requirements of the contract. Subd. 2. **Notice when producer breaches contract.** Except as provided in subdivision 3, if a producer fails to comply with the provisions of a contract that requires a capital investment subject to subdivision 1, a contractor may not terminate or cancel that contract until: (1) the contractor has given written notice with all the reasons for the termination or cancellation at least 90 days before termination or cancellation or as provided in subdivision 3; and (2) the recipient of the notice fails to correct the reasons stated for termination or cancellation in the notice within 60 days of receipt of the notice. Subd. 3. **Immediate effect of notice.** The 180-day notice period under subdivision 1, clause (1), and the 90-day notice period and 60-day notice period under subdivision 2, clauses (1) and (2), are waived and the contract may be canceled or terminated immediately if the alleged grounds for termination or cancellation are: (1) voluntary abandonment of the contract relationship by the producer; or (2) conviction of the producer of an offense directly related to the business conducted under the contract."



Also, under US state legislations, producer has a right to cancel the contract within three days after conclusion <sup>42</sup>

- whether a party may exercise avoidance or must resort to a court
- whether avoidance affects a particular clause or the contract as a whole
- notice of avoidance, form, content and time limits to give notice
- effects of avoidance: payment of damages, restitution

### **Chapter III – Parties' obligations**

37. This section should initially set forth the various approaches taken in different legal systems to the issue of characterisation of agricultural production contracts and the treatment of mixed contracts. Major consequences derive from whether producer and contractor are deemed to deal under a sale or service agreement, or under another particular legal form regulated under domestic law. A variety of issues would have to be considered, either as the object of contractual stipulations, or under the applicable law – including by mandatory provisions.

38. Consideration ought to be given to an appropriate manner to deal with commodity specific features, and whether it would be appropriate to include a section discussing contracts for particular commodities. <sup>43</sup>

39. A central issue to be considered at all times when discussing parties' rights, obligations and liabilities as well as non performance and remedies, regards the ownership of the goods involved in the production process, whether in the form of inputs – in particular seeds, and young animals but also fertilizers and other goods –, or crop while planted and growing, animals being raised, or crop after harvest, or else regarding by-products, residues, wastes, manure etc. This should clearly be stated in the contract.

#### **A – Default provisions governing parties' obligations**

40. The legal regime applicable to a sale/purchase transaction will most often apply to the supply of the produced commodity to the contractor, as well as to the supply of goods by the contractor (as seller of inputs) when seller undertakes to deliver the designated commodity to buyer and transfer ownership or title against the payment of a price. <sup>44</sup>

41. In this context, typical issues to be discussed will include:

- determination of the designated commodity
- actual time of transfer of title (as set by the parties or provided for under domestic law, with varied solutions) determining transfer of risks and liabilities
- nature and scope of warranties owed by seller, regarding the title transferred or the quality of the goods (whether for general defects or for the particular intended purpose) and whether the seller can waive warranties

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It may be noted that this protection is also found under various franchise laws which require consideration of investments made by a franchisee before a franchiser can terminate a franchise agreement.

<sup>42</sup> See *supra* para. 21 and note 17.

<sup>43</sup> See for example the discussion by Hamilton, *Farmer's Legal Guide ... supra* note 8, in dedicated Chapters for "Grain production contracts" (pp. 84-95), "Livestock production contracts" (pp. 96-110) and "vegetable production contracts" (pp. 111-120).

<sup>44</sup> As a useful reference in the international sale of goods regarding perishable goods, cf. International Trade Center (ITC - UNCTAD/WTO) International Commercial Sale of Perishable Goods : Model Contract and User's Guide <http://www.jurisint.org/doc/orig/con/en/2001/2001jiconen0/2001jiconen0.pdf>

- seller's obligation to deliver conforming goods
- buyer's remedies for seller's non performance: in particular whether buyer can withhold performance *i.e.* not paying the price and not taking delivery (by rejecting the goods), available legal and contractual remedies such as price reduction, specific performance, termination of contract, damages (and how damages will be measured in particular regarding purchase of substitute goods)
- grounds of exclusion of liability for non performance
- buyer's obligation to pay a set price (and issue of price determination) and to take delivery of the goods
- seller's remedies for buyer's non performance (in particular in relation to a wrong rejection of goods and rights of the seller to dispose of the goods)

42. Another example of legal regime which may be involved concerns the supply of services. Many obligations undertaken by producer and contractor in the context of an agricultural production contract would be in the nature of applying skill and providing labour with a view to accomplishing a particular performance in the other party's interest.

- Services provided by producer would typically refer to growing the crop or raising the animals in accordance with particular specifications provided by contractor
- contractor may supply services for example in the form of technical advice regarding the production process or direct intervention such as soil preparation or transportation of the produce in the farmer's interest.
- A number of issues will likewise have to be considered when the obligation or the relationship is found to be governed by the legal regime applicable to services, *i.e.* typical performances undertaken by the parties, whether performance involves best efforts or actual results, related warranties, remedies for non performance etc.

43. Similarly, the other provisions of the legal regime for various specific contracts (lease, bailment, "*maquila*" etc.) may also become relevant depending on the characterisation of the parties' obligations, under the agreement or under the law.

## **B – Contractor's obligations under the contract**

44. The following aspects should be discussed in the context of this section:

### **B1 – Provision of goods and services**

45. Contractor may provide or have an interest in the land and/or in fixed assets and/or in production equipment. Forms and special implications should be discussed.

46. Generally, animals and a range of inputs are supplied by contractor: <sup>45</sup>

- with or without transfer of ownership to producer
- as a performance in kind or as advance payment over future delivery. Price value of inputs and services must be specified
- animals and/or inputs may be supplied by a third party designated by contractor. Possible implications should be discussed in the event of defect of the inputs
- according to specified delivery modalities

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<sup>45</sup> Panama law Art. 138 provides that unless otherwise provided in the contract, contractor will be under a duty to supply seeds, input and technical assistance for the production.

47. Contractor may perform directly certain services in relation with the production *e.g.* soil preparation, harvesting etc. In this context, certain circumstances when contractor provides a large range of services regarding the management of the farm and could possibly be considered as a tenant of the owner of the land would need to be discussed.

48. Contractor may also provide credit facilities

- in kind (provision of inputs) ;
- under payment terms (as advance payment over future delivery);
- other forms such as direct loans or acting as a guarantor in a bank financing transaction.

### **B2 – Provision of services in relation to production**

49. A typical feature of production contracts is the contractor's direction and oversight of the production process. <sup>46</sup> This will be reflected in specific obligations for the producer.

50. Contractor or designated third parties may be entitled to have access to producer's land or facilities, to perform oversight operations or technical interventions as may be needed, such as veterinary assistance. Advance notice and related aspects of such procedures should be discussed.

51. Production contracts may also contemplate contractor's delivery of extension services and training programmes.

### **B3 – Taking over of goods**

52. This section should discuss contractual mechanisms for evaluation the quality of the products (see also section C2 hereunder) and contractor's obligation to apply fair and proper standards and to take receipt of product conforming to specifications.

53. Taking over of goods implies practical interventions to be specified (such as removing the crop or the animals)

### **B4 – Price and payment of price**

54. Price clauses are widely regarded as one of the main reasons why producers enter into production contracts and are one essential element for a successful transaction: a satisfactory price mechanism would reduce defaults and promote trust and compliance.

55. Also, confirming the price to be paid for an agricultural commodity through a price clause may avoid future conflict and litigation. This is felt to be particularly important in contexts where public contract enforcement is unlikely, or prohibitively expensive. This is a challenge faced by contract farming projects around the world, but especially in developing countries.

56. Practice reports show, however, that pricing mechanisms are not always transparent. Poorly drafted price clauses would contribute to contract breach and may lead farmers to misrepresent or misunderstand how the price is calculated. They may also provide ground for manipulations by buyers in order to reduce the amount payable. <sup>47</sup>

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<sup>46</sup> Cataluña law Art. 9(e) refers to contractor's obligation to "undertake the direction and technical management of the farm".

<sup>47</sup> For an overview of various mechanisms and examples, cf. document Doc. 1 – Add. 1 on "Contract farming: price determination and a review of contract clauses".

57. This section should examine price clauses and price fixation mechanisms used in agricultural production contracts, their relative advantages and disadvantages, taking into account the nature of the product and the interests of the parties.<sup>48</sup>

58. Except where prices are regulated under public policy, the parties may choose a variety of mechanisms, including any of the following, and variations and combinations thereof

- fixed prices - flexible prices (based on the changes on the world and local markets)
- prices calculated on spot-market values
- prices on a consignment basis (calculated after the produce has been marketed and sold)
- split pricing (part is an agreed base price and the other part is a final price after contractor has sold the product)
- revenue sharing (profit distributed in agreed proportion between producer and processor)
- minimum price
- price based on performance – Application of bonuses and penalties (on performance and yields)

59. This section should also discuss:

- payment guarantee
- payment terms: on delivery; after delivery; with schedule of payments; an advance payment on a specific number of days after the delivery subject to settlement upon the final determination of the price due; schedule of repayment of loan.
- interests due for delayed payment

#### **B5 – Other obligations**

60. Additional obligations to be considered may refer *e.g.* to:

- complying with public communication requirements
- transfer of technology under licensing agreements
- commitments by contractor regarding development of producer group or rural community for example in the form of financial support to health or educational programmes

### **C – Producer's obligations under the contract**

#### **C1 – Obligations related to management of the farm**

61. This section should consider contractual terms relating to the provision of land, facilities or other fixed assets, in particular:

- the identification of the portion of land and specification of whether delivery under the contract applies to the whole production from the designated land or to a designated quantity;
- the identification of the facilities, and whether particular requirements apply or will apply involving additional investment from the producer;
- producer's title / rights over the land and facilities: issues to be discussed include: the potential interest of landowner over the production contract; tenure insecurity, added credit weakness

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<sup>48</sup> For a presentation and discussion of compensation and payment terms, cf. Hamilton, *Farmer's Legal Guide ... supra* note 8, *spec.* at pp. 40-42 and 60-69.

deriving from lack of collateral and consequences on the contract; no transfer of rights over land under a contract <sup>49</sup>

62. The section should also discuss the extent of producer' obligations deriving from:
- control over the land and assets (typically upkeep of fixed assets for the particular purpose of the contract, compliance with public health and environment requirements, insurance and other related costs)
  - provision of the necessary labour force with related costs and liabilities.

### **C2 – Specifications regarding the commodity**

63. Each particular commodity dealt with under the contract will involve particular and detailed specifications. The future Guide should provide illustrations and possible critical issues to address in the contract.

- Quality refers to compliance with physical property (*e.g.* appearance, size, weight, colour and nutrient content ...) and most often to food safety standards, generally fixed by reference to standards and grading scales <sup>50</sup> expressly stated or incorporated by reference into the contract. Different scales would allow for different quality levels corresponding to different pricing. Evidence of the quality may rely on test or certification procedures, involving objective assessment, and possibly third party intervention. Samples are also used for evidence.
- Quantity may be expressed in number of units or weight. It may refer to the whole production or to a fixed amount. Clauses providing for flexibility in deliveries at contractor's discretion (regarding supplies of animals to producer or crop from producer <sup>51</sup>), and corresponding procedures should be discussed. Procedures should apply to ascertain the quantity on a fair basis, *e.g.* by having both parties being present when the produce is weighted.
- Delivery specifications as to modalities (handling, packing etc.) place and time of handing over

### **C3 – Specifications regarding goods and services**

64. Animals and/or inputs may be supplied and owned by producer

65. Producer would be required to provide certain services involving time, labour and skill in relation to agricultural or husbandry production. This may apply when contractor is the owner of the produce (typically in husbandry production), but may also apply to individual obligations in the context of a sale/purchase transaction. Particular specifications applying to the interventions required during the production process will depend on each particular commodity.

66. A number of obligations may be involved:

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<sup>49</sup> See India Model Act: "Notwithstanding anything contained in contract farming agreement, no title, rights, ownership or possession shall be transferred or alienated or vest in the contract farming sponsor or his successor or his agent as a consequence arising out of the contract farming agreement".

<sup>50</sup> Grading and/or certification procedures may apply to product, production process or producer; they are increasingly standardised and applied at international level in particular for export markets, and may involve third party intervention.

<sup>51</sup> See the description of the "passed acres clauses" which are found in contracts for vegetable production, according to which contractor would be entitled not to harvest or purchase the crop even if it meets the contract standards. Instead producer would receive a portion of the contract price from a pool of funds established by a charge on all growers. in Hamilton, p. 113. See *e.g.* the legislation of Wisconsin on Vegetable Procurement Practices.

- to exclusively use inputs provided by contractor and request delivery when needed
- to comply with contractor's instructions regarding cultural or growing/raising techniques (for example for crop cultivation, time and modes of planting, watering, harvesting etc. or for animal husbandry practices: procedures regarding time, quantity and quality of feed; time of delivery/sale, etc.)
- to comply with technical standards or regulations specified by contractor
- to enable access to land or facilities to contractor or designated third parties in relation to the performance of the contract <sup>52</sup>;
- to provide to contractor information on agreed aspects regarding production process, to keep record of the operations undertaken
- to undertake ancillary operations to production such as handling, packing, storage, transportation
- to take out an insurance (or contribute to an insurance fund) for production loss

## Chapter IV – Contract terms and contractual practices

### A – Contract terms

67. The agricultural production activity entails a number of risks which generally bear upon the producer and impact on producer's ability to comply with his obligations under the contract or under the law. Risks derive from the operation of its activity with exposure to weather conditions or death or disease of animals where a clear determination of the origin of events may depend on factual circumstances. How risk elements are contemplated in contracts can vary greatly and are related to other elements, in particular price mechanism.

68. This section should discuss the general principle of parties' autonomy to agree on the content of obligations and on the allocation of liabilities, and the limits to such autonomy under mandatory provisions of domestic legislation depending on the legal nature of the particular obligation or contractual form involved.

69. Examples of clauses frequently found in agricultural contracts will be discussed in this context.

In agricultural production contract practice, many contract terms are reported that are likely to make the performance of the contract particularly onerous or risky for producer. <sup>53</sup>

Typical examples are

- clauses allowing contractor to unilaterally determine certain factors regarding the performance of the contract, applicable remedies and penalties, or termination events; or to change terms and conditions without the consent of the producer;

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<sup>52</sup> Cataluña law Art. 10(f).

<sup>53</sup> Cf. Miller, *supra* note 6, at p. 73 : "One of the troubling aspects of many agricultural production agreements is the apparent attempt by the offeror of the arrangement to shift risks and liability to the producer in amounts and types beyond which any party to the transaction should ordinarily anticipate or accept. This can manifest itself in such areas as requiring unattainable non-genetically modified organism ("non-GMO") levels in grain, making the producer liable for any and all damages associated with commingling of non-GMO and Genetically Modified Organism ("GMO") grain, requiring different testing procedures at different stages of the handling process, being able to terminate contracts virtually at will, requiring the producer to be in compliance with state statutes in states far from the production area, and giving undue access to the producers fields and buildings", also with examples of unfair clauses.

- clauses that waive warranties bearing upon contractor under the applicable law and exclude or limit contractor’s liability for damage resulting from inputs he provided or from contractor’s intervention in the production process and that he might otherwise incur;

70. This section should consider and discuss how such clauses are treated under domestic law. When contrary to mandatory provisions such clauses are unenforceable. Additionally national law provisions may exist to sanction contract terms that are excessively imbalanced or unfair to one party.<sup>54</sup> In certain instances, rules regulating unfair terms may be found in special legislations applicable to particular areas, such as certain “economic activities”<sup>55</sup> or applicable to “merchants”.<sup>56</sup> Also the application of general principles of law, in particular good faith and fair dealings, may be used by courts to sanction unfair clauses.

71. Legislations on agricultural production contracts have used various approaches to deal with unfair contract clauses:

- by making express reference to general contract law,<sup>57</sup> or to specific relevant provisions under the applicable law;
- by making an express reference to an obligation of good faith<sup>58</sup> or prohibition of “unfair clauses”<sup>59</sup>; or unfair clauses will be contrary to the fundamental principle of risk sharing enshrined in certain legislations on production contracts<sup>60</sup>

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<sup>54</sup> This concept is diversely dealt with under domestic law. In the US, the doctrine of “unconscionability” may applied by the court when “in light of the general commercial background and the commercial needs of the particular trade or case, the clauses involved are so one-sided as to be unconscionable under the circumstances existing at the time of the making of the contract” (official comment to UCC §2-302); see discussion in Hamilton, *Farmer’s Legal Guide ... supra* note 8, at p. 30. This is even more likely to be found regarding “adhesion contracts” “if there is a great disparity of bargaining power combined with terms that are unreasonably favorable to the party with the disparate bargaining power” see Miller, *supra* note 6, p. 70.

However, when a legal concept is contemplated under national law to sanction overly imbalanced clauses, restrictions may apply for contracts involving a contingency over future, uncertain events where the parties may be considered to have accepted a certain apportionment of risks (see *e.g.* in France the concept of *lésion*). For a proposal of a general definition in the context of international commercial contracts, see the *UNIDROIT Principles of International Commercial Contracts 2010*, Article 3.2.7 – “Gross disparity”: “(1) A party may avoid the contract or an individual term of it if, at the time of the conclusion of the contract, the contract or term unjustifiably gave the other party an excessive advantage. Regard is to be had, among other factors, to (a) the fact that the other party has taken unfair advantage of the first party’s dependence, economic distress or urgent needs, or of its improvidence, ignorance, inexperience or lack of bargaining skill, and (b) the nature and purpose of the contract”.

As to exemption clauses, reference may be made to *UNIDROIT Principles of International Commercial Contracts 2010*, Article 7.1.6 – “A clause which limits or excludes one party’s liability for non-performance or which permits one party to render performance substantially different from what the other party reasonably expected may not be invoked if it would be grossly unfair to do so, having regard to the purpose of the contract.”

<sup>55</sup> *E.g.* France Code de commerce art. L 442-6 on restrictive competition practices which may find application between commercial parties. Also : in Italy law 192/98 on subcontracting in processing activities (“*subfornitura nelle attività produttive*”) (Art. 9) which provides protection against the abuse of economic dependency characterised by an excessive disparity of rights and obligations between commercial parties. Provisions may however not be applicable when the contract at hand is found to be of a civil character.

<sup>56</sup> See for example in the USA: The Packers and Stockyards Act 1921 (the purpose of which is to ensure that the competition in the livestock, poultry, and meat markets remains fair and efficient) deals with unlawful practices that could affect the distribution and prices of products.

<sup>57</sup> Vietnamese law, Art. 4; Morocco law, Art. 8.

- by considering particular types of contract clauses, such as:
  - penalty clauses or termination clauses <sup>61</sup>
  - confidentiality clauses <sup>62</sup>
  - clauses waiving any producer right or any contractor obligation established in the special legislation. <sup>63</sup>

Such clauses may entail (see also the section on avoidance *supra* para. 36)

- the unenforceability or avoidance of the particular clause <sup>64</sup>
- the avoidance of the contract <sup>65</sup>
- the reformation by the court of the particular clause <sup>66</sup>

## B – Contractual practices

72. Agricultural production contracts are based on close relationships involving reciprocal performances, where trust, fair conduct and cooperation between parties play a central role. However unfair conducts and behaviours are reported to occur in the course of contract performance, where – typically – contractor's unfair behaviour may take a variety of forms.

73. It may be noted that the concept of “unfair practices” may be seen under different perspectives. It may encompass situations involving threat, fraud and fraudulent actions, which are diversely characterised under national laws, with varied consequences regarding applicable remedies. Also unfair practice is often treated as including unfair terms (discussed under the section above on

<sup>58</sup> US Producer Protection Act - Section 3. Implied Obligation of Good Faith. An agricultural contract imposes an obligation of good faith, as defined in section 1-201 of the Uniform Commercial Code, on all parties with respect to the performance and enforcement of the agricultural contract. See also Minnesota Act, Section 17.94.

<sup>59</sup> Panama law Art. 46: “Unfair clauses or clauses waiving or limiting a right recognised under the law are void”.

<sup>60</sup> *E.g.* Cataluña law, Art. 12(1) “the allocation of risks by the parties under the contract shall be determined on the basis of the extent of their obligations”; art. 3(2): “contracts allocating to the producer a greater share of loss than he would receive as remuneration will be void”.

<sup>61</sup> France, Art. 326-5.

<sup>62</sup> USA Farm Security and Rural Investment Act of 2002;

<sup>63</sup> *idem*; see also Model Producer Protection Act 2000, Section xx; and *i.a.* Minnesota Act, Section 9; Minnesota Act, section 17.9443.

<sup>64</sup> Under French law (art. 326-5), clauses contrary to the provisions of the law, penalty clauses and termination clauses will be void. These may be replaced by the provisions of the standard agreement approved by the Ministry of agriculture, if any.

See also *e.g.* US Producer Protection Act: Section 6. And Iowa Act Section 7(b): “[...] The confidentiality provision is void [...]” Section 10 “Any provision of an agricultural contract which waives a producer right or an obligation of a contractor or processor established by this Act is void and unenforceable” ... and “does not affect other provisions of an agricultural contract or a related document, policy, or agreement which can be given effect without the voided provision. [...]”.

<sup>65</sup> Cataluña law, art. 3(2): contracts allocating to the producer a greater share of loss than he would receive as remuneration will be void.

<sup>66</sup> Under French law: see *supra* note 64. Minnesota Act, 17.944 “[...] a court reviewing an agricultural contract may change the terms of the contract or limit a provision to avoid an unfair result if it finds that: [...] the violation has caused or is likely to cause financial detriment to the producer.” And “If the court reforms or limits a provision of a contract, the court shall also make orders necessary to avoid unjust enrichment. Bringing a claim for relief under this subdivision does not entitle a producer to withhold performance of an otherwise valid contractual obligation. No relief may be granted under this subdivision unless the claim is brought before the obligations of the contract have been fully performed.”



contract terms). Finally, unfair conduct will generally be dealt with in the context of non performance, where contractor's wilful misconduct is claimed as a defence to producer's non performance.

74. Following a similar approach to the section relating to unfair clauses, this section should discuss the approach taken under national law to unfair conducts and contractual practices, and how they are sanctioned.

75. The following examples are practices contemplated specifically and in detailed form by US state legislations on production contracts.<sup>67</sup> They refer to "any contractor or processor knowingly to engage or permit any employee or agent to engage in the following practices in connection with agricultural contracts". The following provides a summary of the sections referring to "unfair practices for agricultural contracts" and "Penalties and Enforcement"<sup>68</sup>

- "First, it makes it an unfair practice for a contractor or processor to take action to coerce, retaliate, or discriminate against a producer for the exercise of a "producer right." Producer rights include (1) the right to join a producer association, (2) the right to contract with a producer association, (3) the right to be a whistleblower, (4) the right to exercise rights created by this Act (*i.e.* the right to use a production contract lien, the 3-day right to review production contracts, and the right to disclose contract information). Types of coercive or retaliatory actions are outlined, including alteration of termination terms, payment terms, or contract inputs (e.g. providing sick hogs).
- Second, it makes it an unfair practice for a contractor or processor to provide a producer false information about producer rights or about producer associations.
- Third, it makes it an unfair practice for a contractor to refuse to provide a contract producer information used to determine compensation and to allow a contract producer to observe weighing used to determine compensation.
- Fourth, it makes it an unfair practice for a contractor to use so-called "tournament" compensation programs. Tournament compensation programs base compensation of one contract producer on the performance of other producers. The programs are widely used in the poultry industry and there have been many allegations that the programs allow contractors to unfairly discriminate against producers. The concern is that contractors who control the quality of contract inputs can control, and perhaps unfairly manipulate, a producer's performance under a contract.
- Fifth, it makes it an unfair practice to violate other provisions of the Act, including the disclosure and readability requirements, the prohibition on confidentiality, the mediation provisions, and the prohibition on waivers.

Contractors or processors committing unfair practices under the Act would be subject to both civil and criminal penalties. Importantly, the Act creates a private right of action for producers and awards attorneys fees to prevailing plaintiff producers. This will encourage attorneys to take meritorious cases and will enable producers to seek redress for abuses. The section also grants primary enforcement authority to the Attorney General."

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<sup>67</sup> See US Model Producer Protection Act Section 9; Iowa Act, Section 9. Minnesota Act provides that the commissioner may adopt rules to implement sections 17.90 to 17.98, including the prohibition of specific trade practices.

<sup>68</sup> Quoted from a "Section by Section Explanation Producer Protection Act", office of the Attorney General, Iowa Department of Justice, accessible at :  
[http://www.state.ia.us/government/ag/working\\_for\\_farmers/2000\\_news/producer\\_protection\\_act.html](http://www.state.ia.us/government/ag/working_for_farmers/2000_news/producer_protection_act.html)

76. One other legislation on production contracts refers specifically to the following contract practices:

- contracting with producers already under a contract with another contractor
- committing trade frauds in the determination of quality standards and quantity of commodity farm produce;
- taking advantage of the contractual monopoly to buy at prices below the contractual prices

and “depending on the nature and seriousness of the violations” provides for “compensation for all material damage caused by their acts of violation according to the law provisions on contracts” and for “termination or suspension by the competent State body of the right to trade” or provide for reputational sanctions in the farm produce items which the enterprises have violated, and announce on mass media the contractual breaches by the enterprises.<sup>69</sup>

## **Chapter V – Non performance and remedies**

77. Many circumstances may affect the parties’ ability to perform the contract in accordance with its terms, and an overview of typical situations is presented below, regarding both contractor and producer’s non performance. Similarly to Chapter referring to parties’ obligations, this Chapter should envisage contractual provisions relating to non performance events and applicable remedies, and should also consider the approach taken under the applicable law especially when mandatory provisions may be relevant.

### **A – Non performance of parties’ obligations**

78. In the context of agricultural production contract practice, a common ground of non performance by parties is reported to result from changing circumstances over the life of the contract going beyond the risks contemplated at the time the contract was concluded and profoundly altering the equilibrium of the relationship. Such situations may derive for example from extreme fluctuations in the market affecting prices or supply needs, or drastically more onerous production conditions. This would entail serious consequences over the continuation of the contract and would generally induce the disadvantaged party to breach the contract.

79. The future Guide should consider how parties may deal with this situation for example by including in the contract a provision for a revision of the terms of the contract under specified circumstances. It should also examine whether and how national legislations deal with changes in contract conditions.<sup>70</sup>

#### **A1 – Non performance of contractor’s obligations**

80. This section should discuss typical forms of non-performance of producer’s obligations. Situations where the breach amounts to unfair practices have been dealt under Chapter IV above.

- failure to deliver goods or services, or delivery of defective goods or services

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<sup>69</sup> Vietnamese law, Article 5; and Article 4 also providing that “Enterprises must not compete to buy commodity farm produce of peasants who have got investment from other enterprises for production development; must not sign commodity farm produce-sale contracts with the producers who have already signed such contracts with other enterprises”.

<sup>70</sup> The question whether *pacta sunt servanda principle* could be subject to exception under certain domestic laws in the context of agricultural contracts is to be explored. See as a point of reference the provision on *Hardship* under the *UNIDROIT Principles of International Commercial Contracts 2010*, Art. 6.2.2.

- failure to pay the agreed price. Special consideration should be given to the situation where contractor withhold payment for alleged producer's non performance (see below section A2).

81. Contractor's failure to pay after the produce was delivered is a major risk for producer, especially when contractor is the owner of the goods. The protection that producer may enjoy (as a seller or otherwise) under the applicable law should be discussed in this context. Also delayed payment is very frequent and pose major challenges to producers.

82. It should be noted that certain US state legislations have introduced important protective provisions for the producer in the event of contractor's default:

- a producer who makes a prepayment for agricultural production inputs may demand a letter of credit or bank guarantee from the provider of the inputs to ensure reimbursement if delivery does not occur;<sup>71</sup>
- in case of non performance by contractor, a parent company may be liable to a seller for the amount of an unpaid claim or contract performance;<sup>72</sup>
- producer has a first priority lien for amounts due under a production contract involving livestock, raw milk, or crops. The lien can be enforced against the commodity, the cash proceeds of sale of the commodity, or the property of the contractor.<sup>73</sup>

## **A2 – Non performance of producer's obligations**

83. This section should discuss typical forms of non-performance of producer's obligations.

Contract provisions often deal with producer's non compliance with requirements as to quantity, quality, time of delivery etc. and set contractor's remedies. Many issues will not be fully contemplated in the contract. In this context, issues to be considered include:

- late (or early) delivery, and consequences
- what procedures are in place to ascertain default and extent of default: whether both parties or a third party are involved.
- whether producer is given an opportunity to cure the default, how and under what conditions
- upon alleged defects in quality of the produce, contractor/buyer frequently reduces the price set in the contract, or applies a penalty. Issues should be discusses of how much the price can be reduced or the penalty applied, and how seller can object.
- upon alleged defects in quality of the produce, contractor/buyer frequently rejects the produce (or part of it) by not taking delivery and withholding payment. Several aspects must be considered such as:
  - conditions to reject; in particular, ascertained default, notice to producer
  - consequences of rejecting; whether additional time is available to producer to cure the default (by delivering conforming goods); whether and how seller can object to the reject, and

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<sup>71</sup> Minnesota Act, Section 17.97.

<sup>72</sup> Minnesota Act, Section 17.93 Subd. 2. Under Subd. 1 "If a contractor is required to obtain a license to purchase agricultural commodities, the licensing authority may require the parent company of a licensee subsidiary to guarantee payment or contract performance as a condition of licensing".

<sup>73</sup> See Model Producer Protection Act, Section 8; Iowa Act, Section 7 establishes a first priority lien for a producer for amounts due under a production contract involving livestock, raw milk, or crops. The lien can be enforced against the commodity, the cash proceeds of sale of the commodity, or the property of the contractor. The lien is perfected by filing a financing statement with the secretary of state and terminates one year from the date the commodity is no longer under the authority of the contract.

consequences regarding losses incurred by producer; whether producer can dispose of the rejected goods;

84. A frequently reported breach by producer relates to extra-contractual sale (“side-selling”): under this practice, instead of supplying all the production to contractor as agreed under the contract, farmers would rather sell the produce on the open market to obtain a better price. Also, producers may divert inputs provided by contractor for personal use or for selling them (or producers might purchase crops on the market and deliver under the contract to obtain more favourable prices – with issues of non conforming quality of product).<sup>74</sup>

85. This section should discuss the various manners in which this occurs and is dealt with under contract practice. Consideration will be given to the relation of this practice with pricing issues and changes in circumstances between the time when the contract is concluded and delivery.

86. The agricultural production activity entails a number of liabilities which will bear upon the producer as a matter of law. It will generally be so regarding obligations to comply with public regulations regarding hygiene requirements, food safety, environmental and labour conditions. Aspects related to non compliance with such obligations, and the possible implication of contractor should be discussed in this section.

## **B – Remedies**

87. A number of remedies for non performance may be available to the parties either under the contract or under the applicable law. Discussion regarding the individual remedies should also include how they would apply. As for the other Chapters, special consideration should be given to relevant provisions of special legislations on agricultural production contracts.

88. A number of remedies will generally be available to the parties, either to the defaulting party, or to the non defaulting party depending on the circumstances. They include:

- a party may withhold performance when the other party has not performed: this situation is likely to occur in a variety of situations in an agricultural production relationship where both parties make reciprocal deliveries of goods and services<sup>75</sup>
- party in breach may cure non performance and deliver a conforming performance, under certain conditions
- party in breach may be granted additional time to deliver a conforming performance, under certain conditions
- a party may request specific performance when the other party has not performed, under certain conditions
- terms limiting or excluding liability: see discussion above under Chapter IV A on contract terms.

89. *Force majeure* clauses are frequently included in contracts. *Force majeure* events are generally characterised as being unpredictable, inevitable, beyond the reasonable control of the

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<sup>74</sup> Vietnamese law, Article 6. “Producers can sell their contractual commodity farm produce to other enterprises only when the enterprises which have made investment in the production thereof or have signed commodity farm produce-sale contracts refuse to buy or do not buy out their commodity farm produce”

<sup>75</sup> See also the situation covered by Article 7.1.2 of the *UNIDROIT Principles of International Commercial Contracts 2010* - Interference by the other party – “A party may not rely on the non-performance of the other party to the extent that such non-performance was caused by the first party's act or omission or by another event for which the first party bears the risk”.

parties, and substantially preventing the execution of the contract. They would generally refer to natural events, governmental acts and internal or external disturbances, with a variety of particular situations contemplated by the parties.<sup>76</sup>

90. Upon a *force majeure* event, the affected party is generally excused for non performance. Contractual provisions may cover a number of aspects such as

- notice to be given by the affected party of the impossibility to perform
- partial or temporary impossibility to perform
- continuation of the contract after a suspension period
- the possibility to renegotiate the contract
- measure of loss and allocation of loss between the parties
- right to recover damages

91. This section should discuss the notion of force majeure (also as opposed to risk) and effects in the context of agricultural production contracts and how contractual stipulations are treated under domestic law.

### C – Damages

92. Damages are generally contemplated in the contract.<sup>77</sup> This section should examine parties stipulations and legal provisions applicable to damages. One particular issue to be considered is whether parties may establish freely a compensation or penalty due upon non performance. Approaches will vary depending on the legal system, and considerations in relation with unfair terms and practices may apply in this context.

93. Critical issues to be discussed in relation to damages include:

- allocation of damages based on possible shared liability in the loss
- measure of damage, in particular whether consequential damage is compensable
- amount of compensation
  - whether based on contract price or on market price at delivery time
  - must take into account expenses incurred to limit the loss
- unfair allocation of damages under the contract <sup>78</sup>
- payment of damages and interests due

94. Grounds, forms and effects of other remedies than avoidance, damages and termination that may be applicable in the context of agricultural production contract practice should be discussed in this section.

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<sup>76</sup> See Doc. 1 – Add. 2 on “*force majeure* clauses” reviewing a number of clauses found in agricultural production contracts.

<sup>77</sup> Regarding liquidated damage clause : see Vietnamese law Article 5; Iowa Act, Section 13(c); also France Art. 326-5.

<sup>78</sup> Minnesota Act, 17.944 “[...] a court reviewing an agricultural contract may change the terms of the contract or limit a provision to avoid an unfair result if it finds that: [...] the violation has caused or is likely to cause financial detriment to the producer.” And “If the court reforms or limits a provision of a contract, the court shall also make orders necessary to avoid unjust enrichment. Bringing a claim for relief under this subdivision does not entitle a producer to withhold performance of an otherwise valid contractual obligation. No relief may be granted under this subdivision unless the claim is brought before the obligations of the contract have been fully performed.”

### D - Termination

95. A party may terminate the contract relying on various possible grounds. Agreed termination is often provided for by the parties. This may be discussed under the section of the Guide relating to the duration of the contract.

96. Breach of the contract is a commonly contemplated ground by parties to agricultural production contracts. Contractual practice should be examined, and possible restrictions to enforceability of contract provisions should be discussed. Approaches will vary depending on the legal system, and considerations in relation with unfair terms and practices may likewise apply in this context.

97. One example of such limitation is provided by producer's special protection under US state legislation on agricultural production contract: when producer has been required to make capital investment above a certain amount, contractor may be subject to restrictions on contract termination, avoidance, or failure to renew the contract.<sup>79</sup>

98. Other grounds of termination to be discussed include:

- impossibility of other party to perform
- anticipatory termination in accordance with the contract
- anticipatory breach by the other party

99. Aspects to be considered include:

- notice of termination, form, content and time limits to give notice<sup>80</sup>
- application of contractual damages together with termination
- consequences of termination: restitution

### Chapter VI – Duration and renewal of the contract

100. The duration of the contract, the perspective of having it renewed and the termination conditions are an important part of the risks bearing upon the producer. Agreed termination may be provided for by the parties. The conditions, form and effects of such termination should be discussed in the Guide.

101. Contracts are generally specified to be for a fixed term, generally linked with the biological cycle of production and depends on nature of the crop or husbandry service. There may be a minimum duration under the law.<sup>81</sup> Long term contracts (for crops such as tea, coffee, sugar cane, and cocoa) may require to be amended periodically. Relations between duration of the production contract and producer's land tenure contract should be discussed.<sup>82</sup>

102. As indicated in the context of avoidance and termination (*supra* para. 36 and 97) producer enjoys a special protection under US state legislation on agricultural production contract: when producer has been required to make capital investment above a certain amount, contractor may be subject to restrictions on contract termination, avoidance, or failure to renew the contract.<sup>83</sup>

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<sup>79</sup> See *supra* note 41.

<sup>80</sup> Cataluña law, Art. 8. Notice must be given in writing before the half term of the production cycle.

<sup>81</sup> Cataluña law, Art. 4(2)

<sup>82</sup> Morocco law Art. 9: the production contract cannot be stipulated for a longer period than the land lease contract

<sup>83</sup> See *supra* note 41.

103. Renewal may be subject to express agreement or to automatic renewal (for a specified or unspecified number of times).<sup>84</sup>

## Chapter VII – Applicable law

104. The determination of the applicable law may rely upon different factors. In general, “domestic” contracts, where all (or most) relevant elements are connected with one single country (typically, the location of the parties, the place of conclusion and performance of the contract etc) will be subject to the domestic law of this particular country.<sup>85</sup>

105. Production contracts may conceivably involve a foreign element. Although individual producers will typically contract with a local counterpart, this relationship may be part of a broader commercial pattern with an international dimension, involving different contractual relationships.<sup>86</sup>

106. In case of a dispute, the adjudicating authority may be a State court or an arbitral tribunal (sometimes with a preliminary mediation or conciliation procedure). A State court will usually determine the applicable law in accordance with the conflicts of law rules of the jurisdiction. These may be provided by an international instruments to which the particular State is a party.<sup>87</sup> In determining the applicable law, the particular nature of the relationship (and most often was is to be considered the “characteristic performance”) and its legal characterisation by the judge will be relevant to determine the scope of the obligations of the parties. It is also on that basis that will be assessed the ability for parties to choose the applicable law, and, as the case may be, to derogate from the otherwise applicable law.

107. When the contract is of an international character, the potential application of an international instrument should be considered. In particular:

- The United Nations Convention on Contracts for the International Sale of Goods (CISG) 1980<sup>88</sup>
- The UNIDROIT Principles of International Commercial Contracts 2010.

## Chapter VIII – Dispute resolution

108. Enforcement effectiveness is essential to ensure contractual justice, also to encourage compliance of the contract. However, in many countries action before State courts in case of breach of the contract – either by the farmer or by the buyer – is reported to be unlikely, especially on account *inter alia* of the costs, procedure and the delay the distance from the courts, the negative effects on the relationships between farmers and buyer.

109. Most special legislations contain provisions regarding alternative dispute resolution. Issues to be discussed include:

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<sup>84</sup> France Art. 327-7: except if otherwise provided by the parties, the contract may be tacitly renewed for a maximum period of 1 year. Morocco law, Art. 9.

<sup>85</sup> Country or state. See the provision if e.g. Iowa Act, Section 11, which makes the application of the law compulsory to ensure that producers located in that state will enjoy the protections of the act.

<sup>86</sup> French law - *Code rural* article L631-24 III on “contracts of sale of agricultural products to be marketed or processed”, sets out that it is of mandatory application, and applies to agricultural products delivered in France, no matter the law applicable to the contract.

<sup>87</sup> Within the EU: Regulation 593/2008 of 17 June 2008 on the law applicable to contractual obligations (Rome I); on the American continent: the Inter-American Convention on the Law Applicable to International Contracts.

<sup>88</sup> Cf also the ITC International Commercial Sale of Perishable Goods: Model Contract and User’s Guide: <http://www.jurisint.org/doc/orig/con/en/2001/2001jiconen0/2001jiconen0.pdf>

- purpose and benefits of alternative dispute settlement mechanisms (conciliation / mediation)
- parties may be required to insert a clause providing for mediation; <sup>89</sup> recourse to mediation may also be made mandatory prior to having recourse other binding resolution mechanisms such as arbitration or state court settlement <sup>90</sup>
- most legislations contain provisions relating to the designation by parties of the mediation body or institute/designate a competent authority for settling disputes under such resolution mechanisms (including detailed provisions on the composition, time limits and other procedural aspects) <sup>91</sup>
- a special Authority – and an appellate Authority - instituted under the law may be given exclusive authority to resolve disputes arising out of contract farming agreements <sup>92</sup>
- parties may choose to submit their dispute to arbitration; however, mandatory arbitration proceedings may be restricted or invalid on account of the potential lack of neutrality of arbitrators <sup>93</sup>

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<sup>89</sup> See Iowa Act, Section 12 providing for mandatory mediation

<sup>90</sup> Morocco law, Arts. 12; Vietnam Art. 4 (in fine)

<sup>91</sup> Morocco law Arts. 12-13; Brazilian bill, Art. 5.

<sup>92</sup> India Model Act Art 38. The decision by the authorities "shall have force of the decree of the civil court and shall be enforceable as such and decretal amount shall be recovered as arrears of land revenue".

<sup>93</sup> In the US, under Farm bill 2008, contractors must leave the choice to growers of going to court or using arbitration.