



**Farmers' Guide to**

# **Organic Contracts**

A Publication of Farmers' Legal Action Group

**August 2012**





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Farmers' Legal Action Group, Inc.

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Organic farming has matured over recent decades from the vision of a relatively small number of passionate farmers who operated mostly informally, usually conducting business with a handshake, to a system that is formally codified in statute and increasingly delivered through some of the same formal mechanisms found throughout conventional agriculture. We hope this guide provides the farmers who have made the commitment to organic farming with the information they need as they navigate the organic marketplace, while at the same time growing healthy food that nourishes people, soil, local communities, and the environment.

Susan E. Stokes  
Executive Director and Attorney at Law  
August 31, 2012

*Farmers' Guide to Organic Contracts* can be downloaded for no charge from FLAG's website at [www.flaginc.org](http://www.flaginc.org). Hard copies can be purchased online or by contacting FLAG by telephone at 651-223-5400; by fax at 651-223-5335; by mail at 360 North Robert Street, Suite 500, Saint Paul, MN 55101; or by email at [lawyers@flaginc.org](mailto:lawyers@flaginc.org).





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## INTRODUCTION

The goal of the *Farmers' Guide to Organic Contracts* is to help farmers make informed decisions when evaluating, negotiating, and managing contract agreements with buyers of organic farm products. While fair contracts share benefits and burdens equally between two parties, agricultural contracts in many sectors have historically placed unequal burdens on farmers. Some agricultural buyers deal fairly with farmers, but others take advantage of their superior bargaining power and access to more widespread market information to pressure farmers into signing unfavorable agreements.

This guide aims to help farmers create contracts that allow for stability and predictability within the farmer-buyer relationship while at the same time avoiding contracts that unfairly benefit organic buyers.



FLAG published this guide in response to the growing use of written contracts in the organic sector. The information provided here can assist farmers with all types of agricultural contracts, but our primary purpose is to serve farm operations certified as organic under U.S. Department of Agriculture (USDA) National Organic Program (NOP) regulations.<sup>1</sup> Specific suggestions and information for organic operations are highlighted throughout the guide.

### **CAUTION**

These are educational materials intended for general information only. The information contained in this guide does not constitute legal advice. For advice about your particular situation, consult an attorney who is licensed to practice law in your state.

See Chapter 12 for tips on finding qualified legal counsel.

## CONTRACTS IN THE ORGANIC MARKETPLACE

Although the decision to enter into an organic contract happens on an individual farmer level, these individual contract decisions have a broader impact on the organic community. Consequently, improving contracts for individual farmers could provide meaningful benefits for the organic community as a whole. However, as discussed below, gaining power in the organic marketplace may require farmers to join forces.

### **Growing Organic Market at Risk of “Conventionalization”**

According to the latest census data available, there are more than 14,000 certified organic farm operations in the United States—accounting for over 14 million acres of land.<sup>2</sup> In only 15 years, organic retail sales in the United States have grown from less than \$3 billion to over \$31 billion.<sup>3</sup> Sales of organic products have often increased faster than supply, resulting in shortages of some products.<sup>4</sup> This red-hot growth is projected to continue; at least one forecast predicts the U.S. organic market could be worth almost \$37 billion by 2015.<sup>5</sup>

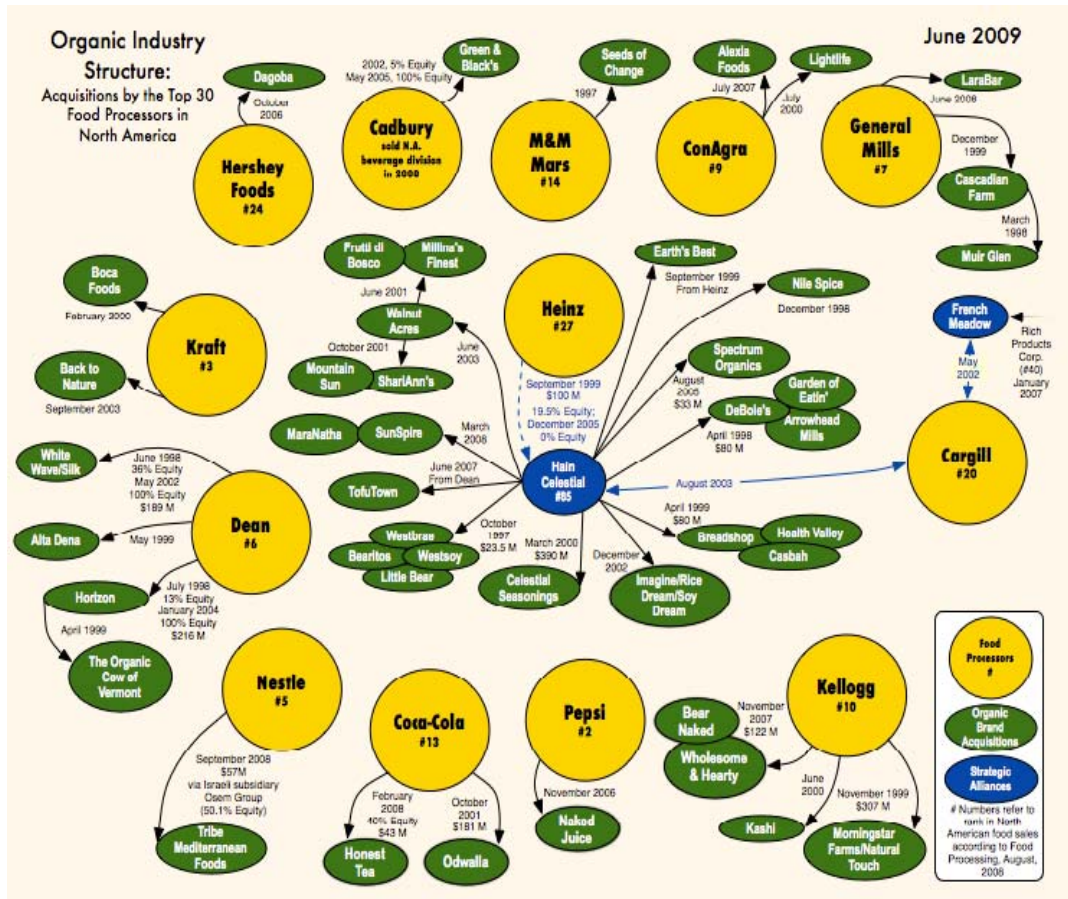
This strong growth comes at some cost, however. As the organic market grows, it is increasingly vulnerable to corporate control and “conventionalization.” As shown in the “Who Owns Organic?” graphic on the next page, over the last 15 years giant agribusiness companies like Kraft, Kellogg, and General Mills have been steadily absorbing smaller organic companies.<sup>6</sup>

From a market perspective, the “conventionalization of organics” refers to large corporations gaining market power by purchasing smaller buyers in the organic market. Having acquired control of a large share of the market and eliminated much of their price competition, these large corporations can lower prices paid to farmers and use contracts to decrease farmer control over production. This “conventionalization” has already occurred in the conventional agricultural market, causing serious financial harm to small-scale farmers, particularly in the poultry and livestock sectors.<sup>7</sup>

The growing concentration of the organic marketplace and the resulting imbalance in bargaining power have already begun to affect at least one group of farmers—organic dairy producers. The organic milk market is largely controlled by a few large corporate dairy processors. As a result, organic dairy producers often report feeling pressured to accept

unfavorable contracts with pay prices that do not cover their costs of production. This happens largely because the lack of competition in the organic dairy market means the large dairy processors have the ability to push down the prices farmers receive.<sup>8</sup>

Who Owns Organic?<sup>9</sup>



Setting a Different Course for Organics

The organic community has an opportunity to set a different course from the conventional industrial agricultural contract model by resisting conventionalization of the organic market and the power imbalances built into that system. One way farmers can gain market power is to join together in farm associations or cooperatives to share information and other resources. The Organic Farmers' Agency for Relationship Marketing (OFARM) (see box below) is one example of organic farmers increasing their market power through collaboration and information sharing.<sup>10</sup>

**Market Power Case Study: OFARM**

OFARM is a marketing-in-common agency comprised of several farmer-member cooperatives and one non-profit firm. While OFARM member organizations are individually responsible for marketing members' farm products, OFARM acts as a central information warehouse, aggregating price and inventory information to help farmers learn the true value of their organic products. As an OFARM brochure says, "Market knowledge is price power." As one recent academic study found, this OFARM-facilitated information exchange allows farmer-members to better predict market conditions. Ultimately, this shared knowledge provides OFARM farmers more leverage with buyers.

In creating farmer leverage, OFARM aims to prevent the conventionalization of organics that occurs when large agribusiness and food corporations break into the organic industry and challenge the control farmers have in pricing. These corporations often have appealing initial prices, but these prices are usually dropped once a corporation secures an advantageous market position. What's more, production contract agreements with these large corporations often increase farmers' risk and decrease their control over their farming operations. In contrast, OFARM aims to offer farmers long-term value by setting floor prices that are profitable for members.

Academic researchers have found that farmers benefit from the strong camaraderie and trust that exists among OFARM members. Members consider OFARM a "neutral place" and share a common goal of sustaining the organic industry. Farmer-members are also able to build reputations as reliable suppliers through joint promotion, sometimes even sending buyers to other OFARM members when they are unable to fill orders. In addition, members gain mentorship and advice from more experienced farmers within the organization.

Formed in 2001, OFARM now spans 18 states and the province of Ontario, making it the largest single organized entity of producers growing organic field crops in North America. Farmers interested in joining OFARM can encourage their marketing group to join OFARM or become a member of one of the current OFARM member organizations. More information is available on OFARM's website: [www.ofarm.org](http://www.ofarm.org).

In the European Union, where organic farming has been a regulated practice for longer than in the United States, countries with strong agricultural cooperatives and other forms of farmer associations have been more successful in resisting conventionalization pressures than

countries without such farmer groups. The strong farmer organization networks have empowered smaller farmers in these countries, helping them access credit, bargain for lower input costs, and access the economic and technical support necessary to compete effectively. At the same time, these forms of organization may have also allowed for higher standards in the treatment of farm labor, as well as more ecologically sustainable methods of production.<sup>11</sup>

Farmers in the United States have the right to associate and form cooperatives (see Chapter 12's discussion of the Agricultural Fair Practices Act (AFPA), page 12–12).<sup>12</sup> As the OFARM example shows, U.S. farmers have the opportunity to copy the success of European organic farmers in resisting the conventionalization of the organic marketplace by joining together to form strong farmer association networks. Farmers may also wish to consider political strategies for resisting conventionalization.<sup>13</sup>

## TO CONTRACT OR NOT TO CONTRACT?

Although written contracts are becoming more common in the organic marketplace, many organic farm product transactions still occur on the spot market through wholesalers or brokers. Thus, it is worthwhile for farmers to consider whether contracting is the right decision for their organic operations.

### **Written Contracts Are Being Offered More Frequently**

While many farmers continue to conduct business on a handshake basis, the use of contracts in agriculture is growing. In 2005, contracts governed 40 percent of the total value of agricultural production in the United States.<sup>14</sup> In comparison, contracts governed only 28 percent of agricultural production in 1991, and a bare 12 percent in 1969.<sup>15</sup> These percentages include both conventional and organic production.

Compared to conventional farmers, organic farmers use written contracts much more frequently. In 2007, almost half of all organic transactions (46 percent) were conducted using written contracts. Slightly less than one quarter of organic transactions were conducted under oral agreements or ongoing handshake relationships between farmers and buyers. The remaining share of organic production was acquired in the spot market.<sup>16</sup>

### **Organic Integrity Concerns and Larger Buyers Lead to More Written Contracts**

It makes sense that written contracts are popular in the organic market. The USDA Certified Organic label was developed in part so that consumers could trust that the food they feed their families was produced without harmful pesticides, hormones, genetically modified organisms (GMOs), and other common conventional agricultural practices. The confidence consumers have in the organic production process translates into higher prices for organic products, which is often referred to as the “organic premium.” Emphasizing the importance of quality in the organic sector, nearly all organic contracts in 2007 (the most recent year for which such information is available) included minimum quality standards and specific quality testing protocols.<sup>17</sup>

As the organic sector booms, however, relationships between organic farmers and buyers have become increasingly formalized. Informal contract arrangements (oral or written) tend to persist over time because the parties have repeated interactions, a high level of trust, and a desire for a long-term business relationship. These informal agreements are more likely to occur between smaller-scale farmers and smaller-scale buyers. In contrast, larger-scale buyers are more likely to use formal written contracts to procure organic farm products.<sup>18</sup> Farmers who once had informal, long-standing relationships with small- or medium-sized buyers often end up working with larger agribusiness corporations that absorb these smaller buyers.

### Realities of Negotiating With Buyers

The combination of organic integrity concerns and a trend toward larger-scale buyers means that organic farmers who might have been used to handshake agreements or short written agreements—with an understanding that unwritten terms would be fleshed out as needed by a mutually acceptable application of common sense, reference to the parties' past dealings, or by a simple phone conversation—are now being presented with complicated written contracts, including a long list of provisions addressing numerous aspects of the farmer-buyer relationship. This trend also means it is becoming increasingly important for organic farmers—who most likely don't have a contract lawyer on staff—to be familiar with the technical ins and outs of contracting.

Generally, whether a buyer will agree to negotiate the terms of a contract offer will depend on a combination of: (1) the strength of the farmer's bargaining power; and (2) how important the particular contract provision is to the buyer.

In the organic market, farmers are likely to have more bargaining power if they produce a scarce, desirable product or can supply products of exceptionally high quality. However, even when dealing with organic farmers with strong negotiating power, buyers are unlikely to agree to contracts made up solely of provisions that are in the farmers' best interest.

Farmers will likely have to accept some provisions that they do not like or that place more risk upon the farmers' shoulders. What farmers should aim for, then, is a contract that has a fair division of risk between farmer and buyer. Oftentimes, buyers who allow farmers to participate in the contract formation process (rather than simply handing the farmer a completed document) are more likely to propose contracts that fairly distribute risk.

## **Pros and Cons of Written Contracts**

Organic farmers most often consider signing written contracts to reduce their uncertainty. Written contracts reduce uncertainty about whether the farmer will have a buyer and the price that will be paid for the organic farm products. From a legal perspective, the biggest advantage of written contracts is that they are generally enforceable in court if a problem arises. In contrast, handshake deals and oral agreements are generally not enforceable in court, although deals that are confirmed in writing or made by exchange of written purchase orders are often considered enforceable. (See Chapter 1 for more information on contract enforceability.)

Contracts can also give organic farmers a greater sense of stability (especially when signed before beginning production) and can allow for more accurate business planning. Contracts can bring higher prices for premium products and may provide an opportunity to raise high-value specialty crops.

In addition, contracts can sometimes serve as a form of risk sharing, especially with respect to price. Farmers who sign contracts prior to harvest can be protected from drops in market price if the contract price at harvest is higher than the market price. Written contracts can also help organic farmers make sure they have thought through all aspects of the farmer-buyer relationship, including issues like preventing contamination in transport, GMO rejection levels, and dispute resolution. Finally, contracts can help farmers access loans for operating expenses, equipment, and even land purchases by providing evidence of a steady source and level of farm income.

Although contracting can help organic farmers manage risk and uncertainty, the mere act of signing a contract creates a certain level of risk. Entering into a contract means taking on very serious legal obligations that can be enforceable in court. Judges typically require people who make contract agreements to keep their contract promises, even if it means they will suffer significant hardship like losing a farm or declaring bankruptcy.

Furthermore, as complex contracts become more common, organic farmers are making an increasing number of promises each time they sign a contract. Each new promise creates a new way that the farmer could breach the contract—whether or not the farmer intends to breach or is even aware of the breach—which could cause the buyer to terminate the contract, withhold payment, sue for damages, or all of these. This guide can help you navigate the extra promises often involved in increasingly complex organic contracts.



In every case, before entering into a written contract agreement, farmers should seriously consider whether the contract provides significant benefits over selling organic products in the spot market.

## HOW TO USE THIS GUIDE

The *Farmers' Guide to Organic Contracts* is meant to be useful to farmers at every stage of the contract relationship. It can help farmers:

- Evaluate contract offers
- Negotiate contract terms
- Manage contract performance, including successfully changing contract terms during the life of the contract
- Find solutions to contract disputes

The following is an overview of the guide's most helpful features.

### **Main Features of the *Farmers' Guide to Organic Contracts***

In developing this guide, FLAG interviewed organic farmers about their experiences with written contracts, reviewed written organic contracts, consulted with leaders in the organic farming community, and conducted extensive research into the laws and policies governing organic farm production and marketing. This investigation led us to offer the following six features in an attempt to make the guide of the greatest use to farmers considering organic contracts.

#### 1. Overview of Contract Laws Relevant to Farmers

Chapter 1 of the guide provides a basic overview of the aspects of contract law likely to be most relevant to farmers. Although farmers don't need legal training to read or sign a contract, a basic understanding of contract law can benefit farmers during contract evaluation, negotiation, and performance—as well as in case of a dispute.

Farmers might be particularly interested in learning how to create an enforceable agreement without signing a formal written contract, as well as how to successfully change an agreement while the contract is ongoing.

## 2. Practical Contracting Toolkit

Chapter 2 of the guide offers practical tools and information farmers can use to analyze and negotiate an organic contract offer. The Quick Organic Contract checklist can serve as a guide for evaluating contract offers, helping farmers consider how the various contract provisions will affect their organic farm operations. In order to allow farmers to quickly access more information about the topics on the checklist, each checklist question includes page references to the parts of the guide that provide more detail about the issues related to each question.

Chapter 2's toolkit also includes a quick primer on contract basics, negotiation strategy tips, and advice about how to successfully manage an existing contract agreement.

## 3. Explaining How Organic Regulations Interact with Contracts



In addition to covering the wide range of contract issues that all farmers should consider, the guide focuses on how organic contracts interact with the unique production challenges of organic farming. An organic contract reflects the fact that special organic farming requirements exist over and above the challenges inherent in all farm operations. To help farmers handle this additional complexity in organic contracts, the guide specifically addresses how contracts can affect farmers' compliance with organic regulations—and how organic regulations can affect farmers' ability to satisfy contract requirements. The guide also provides examples of contract provisions that could help farmers protect organic integrity throughout all stages of production. Note that the guide uses the green leaf symbol pictured here to identify the contract issues that are unique to certified organic operations.

## 4. Examples of Unfavorable and More Favorable Contract Language



The guide provides numerous examples of contract provisions that are modeled after provisions in the organic contracts we studied and analyzed while writing this guide. The guide explains why farmers should be cautious about some of these types of provisions, and provides examples of more favorable (“better”) language that could potentially replace unfavorable (“bad”) provisions. Ideally, farmers can compare the “bad” examples to buyers' written contract offers to identify provisions that should be deleted or changed.

Additionally, farmers can use the “better” examples to craft more farmer-friendly, favorable replacement provisions suited to their operations. The guide uses the symbols pictured here to identify “bad” and “better” example contract language. This symbol system is more fully explained below.

#### 5. Detailed Examination of 100+ Types of Organic Contract Provisions

Chapters 3 through 11 of the guide explore over 100 types of organic contract provisions and include detailed examinations of provisions varying from price to GMO testing to early contract termination to insurance requirements. These chapters are not necessarily intended to be read in one sitting. Instead, farmers can use Chapters 3 through 11 as a reference to answer specific questions as they arise about particular contract provisions.

For example, farmers can use these reference materials to learn about contract terminology they may not recognize or fully understand. These chapters also offer ideas for negotiating to compromise solutions that can allow buyers to address their legitimate concerns while protecting farmers from taking on excess risk.



Farmers can use the guide’s main Table of Contents, Quick Organic Contract Checklist, or individual chapter tables of contents to easily find topics of interest within Chapters 3 through 11. Additionally, each chapter’s table of contents highlights some of the useful tips found throughout the guide. Many tips are flagged with the blue star symbol pictured here.

#### 6. Information About Solving Common Contract Disputes

Chapter 12 of the guide contains information about solving the types of contract disputes that commonly arise in the organic market. This chapter explains how to enforce an organic contract against a buyer, and provides tips for finding a qualified contract attorney and suggestions about how to handle being sued. Finally, Chapter 12 examines the specific legal principles and remedies applicable in ten common contract dispute situations, including rejection of delivered goods, failure to pay, attempts to terminate a contract, failure to keep contract promises, and bankruptcy.

This information can help farmers faced with a contract dispute in negotiating fair, out-of-court solutions from an informed perspective.

## **Explanation of the Symbol System**

The guide contains many example contract provisions in an attempt to help farmers more easily identify in their own contracts the types of provisions discussed here. To allow farmers to quickly identify favorable and unfavorable contract language in this guide, one of the following symbols accompanies each example provision:



Unfavorable contract provision examples (“bad” examples) are most often flagged with a yellow “caution” symbol, meaning that farmers should carefully consider whether the risks created by the provision are worth taking in order to gain the benefits of the contract.

The more rarely used red “stop” symbol identifies provisions that create particularly high risk for farmers, and warns that farmers may wish to reject such provisions due to the risk involved. Farmers are advised to try to negotiate deletion or replacement of these especially risky provisions.



The example contract provisions flagged with the “caution” and “stop” symbols are clearly not meant to be good examples of what fair or well-written contract provisions look like. Instead, they are meant to be examples of what an organic farmer might encounter when considering real contracts in the organic marketplace. As such, they may be unfair, biased in favor of the buyer, or simply unreasonable. Nevertheless, the examples are provided to help farmers understand how to recognize and analyze common organic contract provisions. Farmers should not view them as “model” contract provisions.



The more favorable (“better”) contract language examples are identified with a green “check” symbol. These examples are not meant to be perfect language suitable for every organic contract; they are simply examples of language likely to be more favorable to organic farmers than the provisions flagged with “caution” or “stop” symbols.

**INTRODUCTION — ENDNOTES**

- <sup>1</sup> See generally, 7 C.F.R. Part 205 (2012). The National Organic Program (NOP) regulations are authorized by the Organic Foods Production Act of 1990, 7 U.S.C. § 6501 *et seq.* For more information about the NOP, see the NOP website at <http://www.ams.usda.gov/nop>.
- <sup>2</sup> According to the U.S. Department of Agriculture (USDA) 2008 Organic Survey (the most recent organic census data available), in 2008 there were 14,540 certified or exempt organic farms in the United States, accounting for almost 14.1 million acres of land. The top five states by number of individual organic farms in 2008 were California (2,714), Wisconsin (1,222), Washington (887), New York (827), and Oregon (657). Other states with more than 500 individual organic farms were Pennsylvania (586), Minnesota (550), Ohio (547), and Iowa (518). Close to 2,000 farms were transitioning to organic production in 2008. See U.S. Department of Agriculture, National Agricultural Statistics Service, *2008 Organic Survey* at Table 1 (Farms, Land Use, and Sales of Organically Produced Commodities on Certified and Exempt Organic Farms: 2008), available at [www.agcensus.usda.gov](http://www.agcensus.usda.gov).
- At the end of 2011, the total number of U.S. certified organic “operations” (which includes both organic farms and certified organic processing facilities) was over 17,000. Also at the end of 2011, there were over 28,000 certified organic operations across 133 countries worldwide. See U.S. Department of Agriculture, Agricultural Marketing Service, 2011 List of Certified Operations, available at <http://www.ams.usda.gov/AMSV1.0/getfile?dDocName=STELPRDC5097484&acct=nopgeninfo>. The 2012 Census of Agriculture was ongoing at the time this guide was printed.
- <sup>3</sup> See Council of Economic Advisers, White House Rural Council, and U.S. Department of Agriculture, *Strengthening Rural Communities: Lessons from a Growing Farm Economy*, at 4 (June 2012), available at [http://www.whitehouse.gov/sites/default/files/docs/rural\\_communities\\_06\\_11\\_2012.pdf](http://www.whitehouse.gov/sites/default/files/docs/rural_communities_06_11_2012.pdf).
- <sup>4</sup> Carolyn Dimitri, Lydia Oberholtzer, and Michelle Wittenberger, *The Role of Contracts in the Organic Supply Chain: 2004 and 2007*, at 1, EIB-69, U.S. Department of Agriculture, Economic Research Service (December 2010) (The analysis reported by this study is the first systematic exploration of contract use in the organic sector, and it is based on data from two national surveys administered to firms certified to handle (“process, distribute, manufacture, or repack”) organic products in accordance with National Organic Standards. At the time this guide was written, the study represented the most recent comprehensive data available on organic contracting nationwide.).
- <sup>5</sup> See Sarah Hills, *California is organic ‘land of opportunity,’* Food Navigator-USA.com, March 4, 2011 (stating U.S. organic food and beverage market expected to grow to \$36.8 billion by 2015), available at <http://www.foodnavigator-usa.com/Business/California-is-organic-land-of-opportunity>.
- <sup>6</sup> Changes in the organic industry structure since June 2009 include: (1) Coca-Cola fully acquiring Honest Tea in March 2011; (2) Nestle acquiring Cadbury (and Green & Black’s) in January 2010 and Sweet Leaf Tea in May 2011; (3)

Sara Lee acquiring Aidell's Sausage for \$87 million in May 2011; (4) Perdue Farms, Inc., acquiring Coleman Natural Foods, a processor of organic and natural chicken, in May 2011; (5) General Mills acquiring Food Should Taste Good in February 2012; and (6) Campbell Soup Company acquiring Bolthouse Farms for \$1.55 billion in July 2012.

Philip H. Howard, *Organic Industry Processing Structure*, available at <https://www.msu.edu/~howardp/organicindustry.html>. See also Philip H. Howard, *Organic Industry Structure*, 5 (3) *Media-N: Journal of the New Media Caucus* (Winter 2009), available at [http://www.newmediacaucus.org/html/journal/issues.php?f=papers&time=2009\\_winter&page=howard](http://www.newmediacaucus.org/html/journal/issues.php?f=papers&time=2009_winter&page=howard); see also Philip H. Howard, *Consolidation in the North American Organic Food Processing Sector, 1997 to 2007*, 16(1) *International Journal of Sociology of Agriculture and Food* 13 (2009).

<sup>7</sup> See generally, Amy Guptill and Richard Welsh, *Is Relationship Marketing an Alternative to the Corporatization of Organics?*, *The Natural Farmer*, at 39-41 (Spring 2006); see also Susan E. Stokes, *The Dilemma of Contracting: Risk Management or Risky Business?*, at 1 (Farmers' Legal Action Group, 2006), available at [http://flaginc.org/topics/pubs/arts/CLE\\_SES.pdf](http://flaginc.org/topics/pubs/arts/CLE_SES.pdf).

<sup>8</sup> See, for example, Ed Maltby, *Organic Pay and Retail Price Update for May 2012*, Northeast Organic Dairy Producers Alliance, May 8, 2012, available at [http://www.nodpa.com/payprice\\_update\\_05082012.shtml](http://www.nodpa.com/payprice_update_05082012.shtml). See also Amy Guptill, *Exploring the Conventionalization of Organic Dairy: Trends and Counter-Trends in Upstate New York*, 26 *Agriculture and Human Values* 29 (2009).

<sup>9</sup> Philip H. Howard, *Organic Industry Processing Structure*, available at <https://www.msu.edu/~howardp/organicindustry.html>.

<sup>10</sup> See Organic Farmers' Agency for Relationship Marketing (OFARM) website, available at <http://ofarm.org>. Each OFARM member organization complies with the Capper-Volstead Act of 1922, which established farmers' right to bargain collectively.

For an academic study examining OFARM, see Amy Guptill and Richard Welsh, *Is Relationship Marketing an Alternative to the Corporatization of Organics?*, *The Natural Farmer*, at 39-41 (Spring 2006). See also Thomas Gray, *Organic Federation Seen as a Strategy for Family Farm Survival, Regional Competitiveness*, 79(1) *Rural Cooperatives* at 24 (January/February 2012); see also Organic Farmers' Agency for Relationship Marketing, *Profitable Organic Pricing Starts Here*, available at <http://ofarm.org/assets/Uploads/Brochures/OFARM-Producer-Brochure.pdf>.

<sup>11</sup> See, for example, Charalampos Konstantinidis, *Assessing the Rise of Organic Farming in the European Union, Environmental and Socio-economic Consequences* (Working Paper), University of Massachusetts-Amherst, January 2012, available at <http://www.umass.edu/economics/publications/2012-01.pdf>.

<sup>12</sup> See, for example, the Agricultural Fair Practices Act, 7 U.S.C. §§ 2301-2306 (2012) (discussed further in Chapter 12 of this guide).

<sup>13</sup> Political strategies are a potential tool for resisting conventionalization in the organic marketplace. However, it is important to recognize the limitations of

political strategies at the current time. These strategies have so far made little impact on the conventional agricultural market where political strategies (and litigation) have largely failed to prevent predatory practices by giant agribusiness companies. Most recently, once-promising attempts to strengthen regulation of the poultry and livestock markets to decrease corporate power and protect producers have stalled due to opposition in the U.S. Congress.

- <sup>14</sup> Carolyn Dimitri, Lydia Oberholtzer, and Michelle Wittenberger, *The Role of Contracts in the Organic Supply Chain: 2004 and 2007*, at 1, EIB-69, U.S. Department of Agriculture, Economic Research Service (December 2010). See also Susan E. Stokes, *The Dilemma of Contracting: Risk Management or Risky Business?*, at 1 (Farmers' Legal Action Group, 2006), available at [http://flaginc.org/topics/pubs/arts/CLE\\_SES.pdf](http://flaginc.org/topics/pubs/arts/CLE_SES.pdf).
- <sup>15</sup> Susan E. Stokes, *The Dilemma of Contracting: Risk Management or Risky Business?*, at 1 (Farmers' Legal Action Group, 2006) (citing James MacDonald, *et al.*, U.S. Department of Agriculture, Economic Research Service, No. AER837, *Contracts, Markets, and Prices: Organizing the Production and Use of Agricultural Commodities* 8 (2004)), available at [http://flaginc.org/topics/pubs/arts/CLE\\_SES.pdf](http://flaginc.org/topics/pubs/arts/CLE_SES.pdf).
- <sup>16</sup> Carolyn Dimitri, Lydia Oberholtzer, and Michelle Wittenberger, *The Role of Contracts in the Organic Supply Chain: 2004 and 2007*, at 9, EIB-69, U.S. Department of Agriculture, Economic Research Service (December 2010).
- <sup>17</sup> Carolyn Dimitri, Lydia Oberholtzer, and Michelle Wittenberger, *The Role of Contracts in the Organic Supply Chain: 2004 and 2007*, at 14, EIB-69, U.S. Department of Agriculture, Economic Research Service (December 2010).
- <sup>18</sup> Carolyn Dimitri, Lydia Oberholtzer, and Michelle Wittenberger, *The Role of Contracts in the Organic Supply Chain: 2004 and 2007*, at i, EIB-69, U.S. Department of Agriculture, Economic Research Service (December 2010).



# 1

## Organic Contract Basics

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### CHAPTER QUICK TIPS

#### **Writing Requirement**

Oral agreements (such as handshake agreements) are generally unenforceable in court. Contracts worth \$500 or more must be in writing or they are not enforceable in court. Any changes to contracts must also be in writing to be enforceable.

#### **Special Rules for Merchant Farmers**

You are probably a merchant farmer and special contract rules apply to merchants. Contract law generally holds merchants to a higher standard than non-merchants, loosening some of the formal contract requirements and assuming that merchants will be able to protect their own interests in a contract relationship.



## ORGANIC CONTRACT BASICS

The purpose of this chapter is to educate farmers about the basic legal concepts most likely to be important for farmers entering into organic contracts.

The chapter will cover: (1) basic legal principles involved in contracting; (2) how to form enforceable contracts; (3) how to successfully change contract terms; (4) practical tips for creating enforceable contracts with fair terms; and (5) the truth about common contract myths.

### **IMPORTANT NOTE:**

This guide is not a substitute for an attorney who can analyze the facts of your particular contract or legal situation. If you are a farmer negotiating an organic contract or involved in an organic contract dispute, please make sure to consult an attorney licensed to practice law in your state.

See Chapter 12, page 12-4, for tips on hiring an attorney.

## **BASIC TERMINOLOGY AND CONCEPTS**

### **Organic Contracts**

When this guide refers to “organic contracts” or “written organic contracts,” we mean written contracts governing the sale of any organic crop or commodity.

### **Contract Formation**

Creating or “forming” a contract requires three steps: (1) an offer; (2) acceptance; and (3) consideration (exchange of value). An offer is an indication of intent to be contractually bound upon acceptance by another party. This means one party’s offer gives the other party the power to form a contract by accepting the offer.<sup>1</sup>

Consideration simply means that when you make a contract promise, you must be getting a promise in return. There must be some exchange of value between the parties. For example, your promise to deliver organic products to a buyer is consideration for the buyer’s promise to pay you the organic market price for the products, and the buyer’s promise to pay you is consideration for your promise to deliver.

In addition, a written contract should identify: (1) the parties to the contract; (2) the price to be paid for the goods and/or services to be exchanged; and (3) the quantity of goods to be delivered and/or scope of services to be provided. Any writing (or combination of writings) with these three pieces of information has the potential to create a binding contract (so long as there is also offer, acceptance, and consideration). This can be true even if the writing is not a formal document.

A binding contract can be formed with any type of writing, including a purchase order, an email, notes on a napkin, a ticket, or a letter.<sup>2</sup>

Proper contract formation is very important, but the most common problems with contract formation generally aren’t noticed until later in the relationship when one party challenges the very existence of a contract.<sup>3</sup> This may result from a genuine dispute over whether an agreement was reached, or it may be an excuse to get out of a contract that has become unfavorable or inconvenient.

Looking back to the three steps of contract formation, as discussed above, in order to challenge whether a contract was properly formed, a party

could argue that the offer or the acceptance was invalid, or both, and/or that the consideration given by one or both parties was insufficient. Putting an agreement to sell organic crops or livestock in writing can go a long way toward proving the existence of a properly formed contract.

Even if you have a formal written contract, defending or challenging the formation of a contract often involves very technical legal questions. If you find yourself in a dispute with a buyer over contract formation, consult an attorney licensed to practice law in your state.

### **The Parties to an Organic Contract**

The two parties involved in an organic contract are: (1) you, the farmer; and (2) the buyer.

You, the farmer. This guide is meant for farmers who produce organic crops, dairy products or livestock in accordance with the National Organic Program (NOP) regulations. This includes all farmers who produce U.S. Department of Agriculture (USDA) certified organic commodities (including farmers who may be exempt from USDA certification because they market less than \$5,000 worth of organic farm products per year).<sup>4</sup>

The buyer. The term “buyer,” as used in this guide, means the broad group of individuals and businesses that purchase organic commodities from farmers. Buyers of organic commodities are most likely to be companies that are certified to handle organic products. As of 2007, there were 3,225 certified organic handlers in the United States.<sup>5</sup> These buyers generally purchase organic commodities from farmers and then turn around and sell them further down the organic supply chain, to distributors, retailers (for example, grocery stores), and manufacturers.<sup>6</sup>

Although certified organic handlers (mostly processors, distributors, and manufacturers) make up the largest percentage of buyers, the term “buyer” also includes retailers, co-ops, restaurants, universities and schools, and individuals, such as a neighbor who contracts for organic grain to feed her organic dairy cows. Basically, a “buyer” can be anyone or any company buying the organic commodities you produce.

Buyers of organic commodities are significantly involved in many aspects of on-farm production. In 2007, the most recent year for which data is available, 38 percent of certified organic handlers provided transport for organic commodities, 28 percent provided technical advice on organic requirements, 24 percent provided on-farm production advice, 16 percent provided inputs, 11 percent provided assistance or incentives for organic transition, 9 percent provided labor, and 9 percent provided assistance with organic certification.<sup>7</sup>

## **Sources of Contract Law**

The law of contracts arises from a combination of sources, and is somewhat different in every state. The main sources of contract law are:

- The specific words of your particular contract.
- The common law (case law, or judge-made law) of the state.
- State and federal statutes and regulations. State statutes will usually include a version of the Uniform Commercial Code (U.C.C.). Article 2 of the U.C.C. governs contracts for the sale of goods worth \$500 or more.<sup>8</sup>
- The United Nations Convention on Contracts for the International Sale of Goods (CISG), which governs many transactions for the sale of goods between parties with places of business in different countries.

See Chapter 12 for more detailed information about the federal and state laws that apply to contracts.

## **Oral Agreements (Handshake Agreements)**

Many farmers wonder whether an oral agreement “counts” as a contract. The answer is: “Sometimes.” Although parties are always free to carry out otherwise lawful oral agreements, difficulties can arise when one party wants to force the other to keep contract promises. It is difficult to prove the existence and terms of an oral agreement. If you end up in front of a judge, you will need some type of evidence to prove price, quantity, and other essential terms of the contract. Your chances of success in any legal dispute increase significantly when you can rely on more than just your word against the buyer’s.

Additionally, some agreements (including contracts for products worth \$500 or more) must be written down in some form in order to be binding and enforceable in court (see pages 1–8 and 1–9, next section).

**Key Concept: *Enforceability***

An enforceable contract is a contract that meets all of the requirements of applicable state law and would be recognized as legally binding by a state or federal court. Only enforceable contracts give farmers legal rights against buyers.

Generally, handshake agreements (oral contracts) are not enforceable in court.

Informal contracts are enforceable in court, however, and can potentially include almost anything in writing that has price, quantity, and quality information—such as a purchase order, invoice, email, or handwritten notes.

**Types of Contracts for Sale of Agricultural Products**

Although there are many types of contracts that any farmer will enter into as part of the farming operation, this guide will focus mainly on marketing contracts for organic farm products.

A marketing contract sets a price, price range, or price formula for sale of a specified amount of a commodity. This can happen before, at, or after planting; or before removal of crops, milk, or livestock from the farm. Farmers who enter into marketing contracts: (1) generally own the commodity until it is delivered to the buyer; (2) generally retain the right to make most management and production decisions; and (3) generally bear the risk of loss.

As a general rule, marketing contracts provide farmers more independence than another type of contract common in agriculture: the production contract (discussed below). However, farmers do give up some managerial independence when they agree to sell organic commodities, which must be produced in compliance with the NOP regulations and under organic certification. Additionally, buyers can limit farmers' independence by including burdensome provisions within organic marketing contracts and by becoming more involved in on-farm production.

**NOTE:**

Some farmers refer to certain types of marketing contracts as “full production” contracts, meaning that the farmer has agreed to sell to the buyer the entire production from a defined area (for example, everything produced on 100 acres) rather than a set amount of production. Despite its name, a “full production” contract is still a marketing contract, not a production contract, because the farmer owns the crop until it is delivered to the buyer.

Under production contracts, in contrast to marketing contracts, farmers do not own the crop or livestock product they have agreed to produce. Instead, the owner of the product (often a large company, such as a processor) agrees to pay the farmer for the services required to produce the agricultural product. Production contracts typically allow the owner of the product (the buyer) to make significant management and production decisions. Additionally, production contracts for certain commodities often require the farmer to invest large sums of money in infrastructure (for example, poultry barns) designed or required by the owner/buyer.

Although production contracts have become extremely common (and extremely problematic) in conventional livestock and poultry production, they have yet to be extensively used in organic production. Still, because many organic poultry and livestock handlers are subsidiaries of large conventional agribusinesses (for example, Tyson Foods, Perdue), it is certainly possible that more organic poultry and livestock farmers will be offered production contracts in the future.

**Focus of the Guide**

This guide will focus primarily on marketing contracts. However, FLAG has written extensively about production contracts and other organic marketing activities. FLAG's farmer-friendly publications can be downloaded for free from FLAG's website ([www.flaginc.org](http://www.flaginc.org)), or be purchased in printed form.



FLAG's farmer-friendly publications of interest to organic farmers include:

### **Dairy Contracts**

- Tools for Dairy Farmers in Tough Economic Times (2010)
- When Your Processor Requires More than Organic Certification: Additional Requirements in Organic Milk Contracts (2008)
- Hushed Up: Confidentiality Clauses in Organic Milk Contracts (2008)

### **Livestock and Poultry Production Contracts**

- Contract Poultry Growers Have Rights Under Federal Law (2006)
- Questions to Ask Before You Sign a Poultry Contract (2005)
- Livestock Production Contracts: Risks for Family Farmers (2003)

### **Disaster**

- Disaster Readiness and Recovery: Legal Considerations for Organic Farmers (2007)

### **Marketing**

- Selling Directly to Schools: Tips for Farmers (2010)
- Federal Law Protects Farmers' Rights to Be Paid for Fruit and Vegetable Crops (2007)
- Understanding Farmers' Market Rules (2006)

### **GMOs**

- Farmers' Guide to GMOs (2nd Edition) (2009)
- If Your Farm Is Organic, Must It Be GMO-Free? Organic Farmers, Genetically Modified Organisms, and the Law (2007)

***All FLAG publications are available for free download at [www.flaginc.org](http://www.flaginc.org).***

## **CREATING ENFORCEABLE CONTRACTS**

As mentioned earlier, a contract may be lawful without being enforceable. Lawfulness is determined by the acts or goods that the contract involves. That is, a contract to commit a crime is unlawful no matter how carefully the parties may document their agreement. Enforceability, on the other hand, assumes that the contract is lawful and instead considers whether the agreement can be enforced by law. If a contract is enforceable and a dispute arises, either party can sue the other and seek money damages or a court order forcing the other party to fulfill its obligations.

Enforceability of otherwise lawful contracts is only important if there is a problem. If everything goes smoothly and the contract is carried out to both parties' satisfaction, it doesn't matter whether it would have been enforceable in court. However, because it is impossible to perfectly predict in advance whether problems will arise, enforceability is a very important consideration.

Because contract enforceability often involves very complicated legal questions, you should consult an attorney licensed to practice law in your state if you want to challenge or defend the enforceability of a contract.

### **Contracts Must Generally Be in Writing to Be Enforceable**

Many types of contracts must be in writing in order to be enforceable in court. The laws that require these contracts to be put in writing are generally called "statutes of frauds." This name is somewhat misleading, because statutes of frauds are not laws about frauds; statutes of frauds are intended to prevent fraud by requiring written agreements.<sup>9</sup>

Each state has its own statute of frauds, and the specifics may differ from state to state. However, in almost all states, a contract to sell goods for a price of \$500 or more must be in writing.<sup>10</sup> Crops and livestock, including growing crops and unborn livestock, qualify as "goods."<sup>11</sup> Therefore, since most farmers are contracting to sell organic farm products (goods) worth \$500 or more, organic contracts must generally be written down in some form in order to be enforceable in court.



### **Oral Agreements Are Generally Unenforceable**

If you have an oral contract (like a handshake agreement) for a sale of agricultural products worth \$500 or more, that oral contract will generally be unenforceable in court.

Farmers and buyers are free to perform otherwise legal oral agreements to sell goods worth \$500 or more. But if an agreement falls through, the courts generally cannot enforce a contract unless it is in writing.

Bottom line: If you don't have something in writing—even something very informal, as discussed below—you probably can't enforce your contract against the buyer, and the buyer probably can't enforce the contract against you. However, even if your contract is unenforceable, if you have given the buyer something of value (like crops or livestock) and the buyer won't pay you for it, a court would likely order the buyer to pay you.

### **The Required “Writing” May Be Very Informal**

Although organic contracts must generally be in writing, the “writing” can be extremely informal. All that is required is some writing sufficient to indicate that a contract for sale has been made between the parties. As stated above, the writing can be an email, notes on a napkin, a ticket, or a letter.<sup>12</sup> The contract terms can even be “written in lead pencil on a scratch pad.”<sup>13</sup>

An exception to the writing requirement, for contracts created by the action of the parties, is discussed below.

**NOTE:**

This guide uses the words “terms,” “provisions,” and “language” interchangeably when discussing words, clauses, or portions of text in organic contracts. Thus, the phrases “contract terms,” “contract provisions,” and “contract language” have the same meaning.

**Special Contract Rules for “Merchant” Farmers Apply to Many Farmers**

Special contract rules apply when both parties to the contract are “merchants.”<sup>14</sup> A merchant is defined as “a person who deals in goods of the kind or otherwise by his occupation holds himself out as having knowledge or skill peculiar to the practices or goods involved in the transaction.”<sup>15</sup> Farmers who regularly sell crops, dairy, or livestock are very often considered merchants,<sup>16</sup> and buyers will almost always be merchants. Merchants are assumed to be knowledgeable businesspeople, and contract law generally holds merchants to a higher standard, loosening some of the formal contract requirements and assuming that the merchants will be able to protect their own interests in a contract relationship.

**Forming a Contract Between Merchants: The “Written Confirmation + No Objection Within 10 Days” Rule**

If one merchant sends written confirmation of an oral contract to another merchant, and if the merchant receiving the confirmation has reason to know what the confirmation says, both merchants will be bound by the contract unless the receiving party sends a written objection within 10 days of receiving the written confirmation.<sup>17</sup>

Here’s how the rule works:

**Example: Written Confirmation + No Objection Within 10 Days Rule**

If a merchant buyer:

- (1) Sends you (a merchant farmer) written confirmation of an oral agreement, AND
- (2) You read the written confirmation or have reason to know what the confirmation says, AND

- (3) You do not send a written objection to the buyer within 10 days of receiving the confirmation...

... a contract was formed that binds both you and the buyer.



**Farmers Can Use the “Written Confirmation + No Objection Within 10 Days” Rule to Create an Enforceable Contract**

Parties who are regularly involved in buying and selling a given type of product are considered “merchants.” Both farmers and buyers are often considered merchants. Between merchants, an enforceable written contract can be created if:

- (1) you send to the buyer written confirmation of an oral agreement you have reached,
- (2) the buyer reads it or has reason to know what the confirmation says, and
- (3) the buyer fails to send you a written objection within 10 days of receiving the confirmation.

This is a convenient way to create an enforceable contract if you feel uncomfortable asking the buyer for a formal written contract and the buyer does not object.

Merchants can also create a contract by action, as described on pages 1–14 through 1–16 of this chapter, even if the informal written documents do not form an enforceable contract.

**Forming Enforceable Contracts With Mismatched Writings**

Under traditional contract law, courts required contract offers and acceptances to “mirror” each other. This is called the mirror-image rule. The party who received the offer had to accept the offer “as-is”; if any language was deleted or added, no contract was formed. Instead, the attempted acceptance was considered a rejection and counteroffer.

**The “Modern Rule” Replaces the “Mirror-Image Rule”**

Modern business practices—such as the routine use of standard-form purchase orders and invoices—have made the mirror-image rule unworkable for the sale of goods. Consequently, the mirror-image rule has

been abandoned for contracts involving the sale of goods worth \$500 or more, which includes most contracts for the sale of organic farm products.<sup>18</sup>

The so-called “modern rule” was developed to deal with the common situation in which parties intend to form a contract through the exchange of informal writings that do not match exactly (mismatched forms). For example, a buyer might have a standard purchase order form, and your farm might have a standard acceptance form, or invoice form. It is unlikely that the buyer’s purchase order form and your standard invoice form will use exactly the same language. Still, under the modern rule, an exchange of these mismatched forms can create a contract between you and the buyer.

**Contract Acceptance Can State Additional and/or Different Terms**

For contracts to sell goods worth \$500 or more, a definite and timely acceptance is valid even if it states terms additional to or different from those offered.



**If a Contract Is Formed With Mismatched Forms, What Are the Terms?**

If a contract is formed with an offer (such as a buyer’s faxed purchase order) and an acceptance (such as an email response to the purchase order) that do not match exactly, an important question is: “What are the terms of the contract?” The answer depends on whether the parties are merchants.

If at least one party is a non-merchant, the terms of the contract will be only those provisions that are in both the offer and the acceptance.

If both parties are merchants, the terms of the contract will be the provisions in both the offer and acceptance, plus any additional provisions that:

- (1) do not significantly alter the contract; and
- (2) were not objected to before contract formation or within a reasonable time after contract formation.

If any provisions in the offer and acceptance conflict with each other, it is generally presumed that the parties object, and those provisions will not become part of the contract.<sup>19</sup>

**Example: Determining the Terms of a Contract Created by Mismatched Forms**

Buyer offers a purchase order with terms A, B, and C.

You send back an acceptance form with terms A, B, the opposite of C, and D.

**What are the terms?**

If at least one party is a non-merchant, the terms are:

A and B.

**If both you and the buyer are merchants**, the terms are A, B, and possibly D. D would be part of the contract only if:

- (1) D does not significantly change the contract;
- (2) The buyer has not already objected to D; and
- (3) The buyer does not object to D within a reasonable time after receiving your confirmation.

In most situations, neither C nor the opposite of C would be part of the contract because they are in conflict.

**Exception to the Modern Rule That Mismatched Forms Create a Contract — “As-Is Only” Offer Is Explicitly Limited to Terms**

There is a narrow exception to the modern rule that mismatched forms can create a contract. The exception is for “as-is only” offers that are explicitly limited to their own terms. For example, a buyer might send you a purchase order stating that the offer terms must be accepted “as-is.” In this case, if you send back an acceptance with even slightly different language, no contract is formed by the exchange of the purchase order and your acceptance. To form a contract, you would have to send back an acceptance with language identical to the purchase order, or a statement to the effect that you accept the exact terms of the purchase order. If you send back something even slightly different, no contract is formed.

Farmers can make an “as-is” only offer by explicitly stating that the offer is limited to the terms of the offer, or stating that the offer is extended on an “as-is only” basis. If you make an as-is only offer, though, be aware that the acceptance must exactly mirror your offer. If the acceptance is not identical, no contract has been formed.

### **Exception to the Writing Requirement – Creating a Contract by Action**

There is an exception to the rule that contracts for the sale of goods worth \$500 or more must be in writing in order to be enforceable. The exception is for contracts formed by “action.” Under this exception, even if the parties fail to create an enforceable written contract where a writing is typically required (maybe they made an oral agreement to sell goods worth \$500 or more), an enforceable contract can be formed if the parties act as if a contract exists. This is sometimes called an “implied contract.”

A contract by action is formed and a written agreement is not required if any of the following actions take place:

- the buyer accepts and pays for the goods,  
or
- the farmer (seller) accepts payment for the goods,  
or
- the buyer admits there was an agreement (usually this must be done under oath).<sup>20</sup>

#### **Example: Contract Formed by Action**

A farmer and buyer enter into an oral agreement for sale of 1,000 pounds of organic apples. But the farmer does not follow up with a written confirmation, and neither does the buyer. No enforceable contract was formed.

Nevertheless, the parties act as if a contract exists. The farmer delivers the apples, and the buyer accepts them and pays the farmer for them.

An enforceable contract was formed by the buyer’s action of accepting and paying for the goods.



## **If a Contract Is Created by Action, What Are the Terms?**

If a contract is created by action, it may not be obvious what terms are contained in the contract.

- *Terms of Contract by Action After Oral Agreement*

In the example above, where the farmer and buyer entered into an oral agreement but failed to later form an enforceable written contract, the terms of the contract created by action would be the terms the parties orally agreed upon, with any important gaps filled in by state law (see next page).

- *Terms of Contract by Action After Exchange of Mismatched Forms*

An exchange of mismatched forms might fail to create a contract. For example, if one party's form is "as-is only," and the other party tries to accept with a form that has deletions or additions, no enforceable contract is formed.

If a contract is formed by the actions of the parties after an exchange of mismatched forms, the terms of the contract consist only of the provisions that are the same in each party's form.

Example: Contract Created by Action After Exchange of Mismatched Forms

Buyer offers a purchase order with terms A, B, and C. The purchase order states that the offer is limited to the exact terms of the purchase order.

You respond with an acceptance form including terms A, C, and D.

No contract is formed, because the offer was explicitly limited to its terms, and your acceptance was not identical to the offer.

However, after the exchange of forms, you and the buyer act as if there is a contract. You grow crops for the buyer, and the buyer receives and pays you for the crops. Your actions and the buyer's actions create a contract.

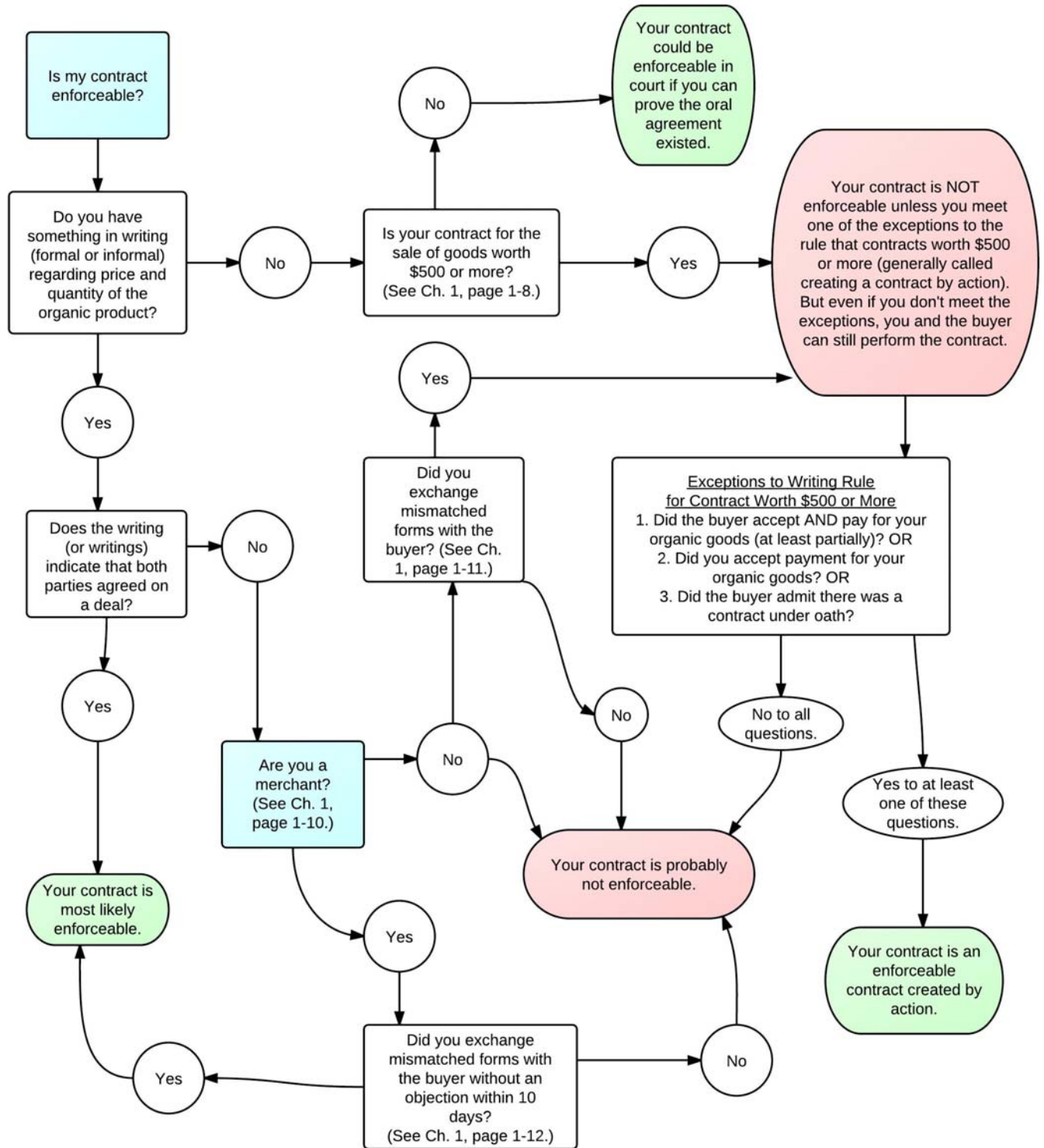
What are the terms of the contract?

The terms of the contract are A and C. This is true because the written documents (the purchase order and the acceptance form) agree upon A and C. Neither B nor D are included in the contract because the documents do not agree on B and D—each term is in only one document, not both documents.

### **Filling in the Gaps**

If important gaps remain in the contract after the agreed-to terms have been established, state law generally provides standard terms that fill in the negotiated contract terms.<sup>21</sup> These supplementary terms might come from your state's version of the Uniform Commercial Code, from other contract law statutes, or from judicial interpretation (case law).

## FLOW CHART: DO I HAVE AN ENFORCEABLE CONTRACT?



## CHANGING CONTRACT TERMS

The terms of a contract are set at the time the contract is formed. However, the terms can later be changed if both parties agree in writing.

Many unexpected things can happen in between contract formation and the final delivery of the contracted goods. It is not uncommon for farmers and buyers to want to change the precise terms of their agreement at some point in the production cycle. Often, this change is discussed during a phone call or in-person conversation between the farmer and the buyer. Much less often, however, does the farmer or the buyer take the crucial step of confirming the agreed-upon change in writing. Failing to confirm in writing an oral agreement making changes to a contract (for example, by sending a written letter to the buyer) is very risky.

### **Get All Contract Changes in Writing!**

It's best to think about contract changes in the same way that you should think about contract formation: Get it in writing! Oral modifications to organic contracts are generally without legal effect.<sup>22</sup>

As with oral contracts in general, farmers and buyers are free to carry out otherwise lawful oral agreements, including oral agreements making changes to an existing contract. However, if a problem arises, it will be the written contract that will control the outcome rather than a later oral agreement. Without a written document establishing the change to the existing contract terms, the change will generally not be enforceable.

## PRACTICAL TIPS

### **Tip #1: If you and the buyer reach an oral agreement, write to the buyer confirming the terms of the agreement.**

If you and the buyer have reached an oral agreement, and you don't feel comfortable asking the buyer for a formal written contract, send the buyer a letter, fax, or email confirming the terms of your oral agreement. If the buyer does not object to the terms set forth in your message within 10 days, you have likely formed an enforceable contract. The contract terms will be those in your written confirmation.

If the buyer responds to your confirmation with a writing of its own that sets out contract terms in addition to or different from the terms in your confirmation, you may still have an enforceable contract unless you respond with an objection within 10 days. If you do not object, the terms of the contract will be the terms your written confirmation and the buyer's written response agree upon, plus any of the buyer's terms that do not significantly change the contract. Any terms that conflict between the writings will not be part of the contract.

Note that you and the buyer could negotiate back and forth within the 10-day window indefinitely. If you write back to the buyer within 10 days of receiving a written confirmation stating you no longer wish to make a deal, no contract will be formed.

Note also that the "Written Confirmation + No Objection Within 10 Days" rule (discussed in detail on pages 1–10 and 1–11 of this chapter) is a two-way street. If you receive a written confirmation of an oral agreement from a buyer, you will likely be bound to the agreement unless you write back and object within 10 days.

### **Tip # 2: If the buyer sends you a contract, but you don't like some of the terms, you can delete and/or add terms and send it back to the buyer.**

If the buyer sends you a written contract, and you do not like some of the terms, you can cross out the terms you don't like and/or write in new terms and send it back to the buyer. If the buyer did not send you the contract on an explicitly "as-is" basis (discussed on page 1–13 of this chapter), and if the buyer does not object to the deleted and/or added terms within 10 days of receiving the marked-up contract, you have likely

created an enforceable contract. The terms are the contract language with your changes.

If the contract was presented to you on an “as-is” basis, meaning the buyer communicated to you that the contract was an all-or-nothing offer, you can still cross out and/or add terms and send it back. However, no contract will be created unless the buyer responds to your marked-up version and accepts it. There is no specific time limit for acceptance. But, even if the buyer does not respond with an acceptance and no contract is created at the outset, if you and the buyer act as though there is a contract (you deliver goods, and the buyer accepts and pays for goods), then a contract has likely been created by your actions. The terms of this contract by action are the terms from the buyer’s original offer that you did not cross out or otherwise clearly reject. The terms you crossed out are not in the contract by action, and if you added terms to the original offer, those terms are also not part of the contract by action. For example, in an original offer with terms A, B, and C, if you crossed out C and added D, the terms of the contract by action would only be A and B.

Note that, at any time, you and the buyer could decide to create a formal contract instead of relying upon the exchange of informal writings or forms. If a formal contract is created, the terms of the formal contract will most likely supersede anything written or orally agreed upon prior to the creation of the formal contract.

## DEBUNKING CONTRACT MYTHS

**Contract Myth #1:** The buyer won't enforce the contract against me, so I needn't bother to negotiate terms with the buyer before signing.

**Truth:** Buyers will enforce contracts against farmers if doing so is in their best interest. Don't assume that the buyer won't enforce the terms of the contract. Negotiate up front and be prepared to comply with all of the provisions of the contract that you sign, or be prepared for the possibility that you may be sued.

**Contract Myth #2:** If I sign a contract while telling the buyer that I don't like some of the terms, or that I won't comply with the terms, the buyer cannot enforce those terms against me in court.

**Truth:** The buyer can hold you to anything written in the contract, even if you tell the buyer before signing that you don't like the language or won't comply with it. Ignoring contract terms doesn't work. In court, only the terms of the written contract matter.

**Contract Myth #3:** If I sign an unfair contract under pressure because I absolutely need the money to keep my farm running, I don't have to abide by the contract terms. The buyer won't let me negotiate, and I have to sign, so I'm not really bound by the terms.

**Truth:** Even if the economic reality is that you absolutely must sign an unfair contract or risk financial ruin, you generally have to comply with the terms of the unfair contract no matter what. Economic duress is generally a losing defense against a breach of contract claim in court.

**CHAPTER 1 – ENDNOTES**

- <sup>1</sup> See, for example, Restatement (Second) of Contracts § 1 (1979); see also U.C.C. § 1-201 (1977).
- <sup>2</sup> See, for example, *Carnival Cruise Lines, Inc. v. Shute*, 499 U.S. 585 (1991) (ticket); see, for example, *Lucy v. Zehmer*, 84 S.E.2d 516 (Va. 1954) (back of a receipt).
- <sup>3</sup> See, for example, *ConAgra, Inc. v. Nierenberg*, 7 P.3d 369 (Mont. 2000) (wheat farmer challenges existence of contract formed by written confirmation of oral agreement).
- <sup>4</sup> See 7 C.F.R. § 205.101(a)(1) (2012).
- <sup>5</sup> Carolyn Dimitri, Lydia Oberholtzer, and Michelle Wittenberger, *The Role of Contracts in the Organic Supply Chain: 2004 and 2007*, EIB-69 at 6, U.S. Department of Agriculture, Economic Research Service (December 2010). The 2007 data are the most recent figures reported by USDA, from the first USDA census of organic agriculture. The 2012 Census of Agriculture was ongoing at the time this guide was written.
- <sup>6</sup> Carolyn Dimitri, Lydia Oberholtzer, and Michelle Wittenberger, *The Role of Contracts in the Organic Supply Chain: 2004 and 2007*, EIB-69 at 8, U.S. Department of Agriculture, Economic Research Service (December 2010).
- <sup>7</sup> Carolyn Dimitri, Lydia Oberholtzer, and Michelle Wittenberger, *The Role of Contracts in the Organic Supply Chain: 2004 and 2007*, EIB-69 at 11, U.S. Department of Agriculture, Economic Research Service (December 2010).
- <sup>8</sup> Louisiana is the only state that has not adopted Article 2 of the U.C.C.
- <sup>9</sup> See, for example, *C.R. Klewin, Inc. v. Flagship Properties, Inc.*, 600 A.2d 772 (Conn. 1991).
- <sup>10</sup> See U.C.C. § 2-201 (2000).
- <sup>11</sup> U.C.C. § 2-105(1) (1977).
- <sup>12</sup> See, for example, *Carnival Cruise Lines, Inc. v. Shute*, 499 U.S. 585 (1991) (ticket); see, for example, *Lucy v. Zehmer*, 84 S.E.2d 516 (Va. 1954) (back of a receipt).
- <sup>13</sup> See U.C.C. § 2-201 comment 1 (1977) (“The required writing need not contain all of the material terms of the contract and such material terms as are stated need not be precisely stated. All that is required is that the writing afford a basis for believing that the offered oral evidence rests on a real transaction. It may be written in lead pencil on a scratch pad. It need not indicate which party is the buyer and which the seller. The only term which must appear is the quantity term which need not be accurately stated but recovery is limited to the amount stated. The price, time and place of payment or delivery, the general quality of the goods, or any particular warranties may all be omitted.”)
- <sup>14</sup> U.C.C. § 2-201(2) (1977).
- <sup>15</sup> U.C.C. § 2-104(1) (1977).
- <sup>16</sup> See 10 Williston on Contracts § 29:25 (4th ed.), at footnote 9 (May 2012) (“[T]he issue of whether a particular farmer may also be classified as “merchant” within the meaning of U.C.C. § 2-104(1) must be determined on a



case by case basis. The court in each case must determine, on the basis of the evidence presented, whether an individual who is considered a farmer also possesses expertise in the area of marketing ... sufficient enough to classify him as a “merchant” within the purview of the Uniform Commercial Code.”); see, for example, *In re Montagne*, 431 B.R. 94, 113 (Bankr. D. Vt. 2010) (determining a dairy farmer is a merchant in all aspects of his mercantile capacity, that is, with respect to goods for dairy farming operations, but not for every purchase of goods).

- <sup>17</sup> See U.C.C. § 2-201(2) (1977); see, for example, *ConAgra, Inc. v. Nierenberg*, 7 P.3d 369 (Mont. 2000) (discussing the merchant exception in Montana’s version of the U.C.C.).
- <sup>18</sup> See, for example, *Gardner Zemke Co. v. Dunham Bush, Inc.*, 850 P.2d 319 (N.M. 1993).
- <sup>19</sup> U.C.C. § 2-207 (1977); see also comment 6.
- <sup>20</sup> U.C.C. § 2-201(3) (1977). Additionally, a written agreement may not be required if the goods were specially manufactured for the buyer and are not suitable for sale to others in the ordinary course of business.
- <sup>21</sup> See, for example, U.C.C. § 2-207 (1977); Restatement (Second) of Contracts § 204 (1979).
- <sup>22</sup> See, for example, *Brookside Farms v. Mama Rizzo’s, Inc.*, 873 F. Supp. 1029 (S.D. Tex. 1995).



# 2

## Practical Contracting Toolkit

- [2-1](#) How to Analyze a Written Contract Offer
- [2-2](#) Quick Checklist for Organic Contracts
- [2-4](#) Seven Rules of Contracting
- [2-8](#) Before Signing on the Dotted Line: Ten Questions
- [2-14](#) Contract Negotiation Strategies
- [2-17](#) After You Sign

### CHAPTER QUICK TIPS

#### **Easy Negotiation Strategy**

Bring an ally to the negotiating table (such as a spouse, friend, relative, or lawyer). That person can provide invaluable moral support, even if they are just there to observe. An ally can also help you buy time to think, because you can ask the buyer to let you and your ally “take a moment” for a private discussion. You can use that private time to gather your thoughts and refocus on your negotiating strategy.

#### **Use A Checklist**

Using a contract review checklist can help make sure you identify and consider the significant risks and benefits of the deal before signing a contract. The Quick Checklist for Organic Contracts is a good place to start.



## **PRACTICAL CONTRACTING TOOLKIT**

This section is meant to be a reference tool for farmers who need quick advice about an organic contract offer. However, it is not meant to cover all of the issues that should be considered in a contract negotiation, and it is certainly not a substitute for an attorney. This toolkit should be seen as merely a starting point for farmers interested in negotiating more favorable contracts with organic buyers.

### **How to Analyze a Written Contract Offer**

- Read through the entire contract.
- Read the contract again at least once; mark it up with notes, proposed changes, and questions.
- Use a checklist to make sure you have covered all the important points (see the Quick Checklist for Organic Contracts on pages 2–2 and 2–3 of this chapter).
- Get answers to your questions (ask the buyer, your attorney, your lender, your organic certifier, etc.).
- Decide what you need to change in order to make the contract worth signing.
- Negotiate with the buyer for the changes and clarifications you want.
- Get all negotiated changes in writing.

## QUICK CHECKLIST FOR ORGANIC CONTRACTS

This checklist is designed to be a list of questions farmers should ask themselves when evaluating an organic contract. Answering the questions will help you more fully understand the risks and benefits involved in the contract. Check off each question after you have answered it to your satisfaction, and use the page references to find more detailed explanations of each topic within the guide. It is not necessary for an organic contract to include all of the topics covered by this checklist, but knowing what is left out of an organic contract can be just as important as understanding what is included in an organic contract.

### Parties & Contract Relationship (Ch. 3)

- Who are the parties to the contract? (3–1)
- Who owns the product being sold—the buyer or the organic farmer? (3–2)
- Is someone else's approval required before the contract can begin? (3–3)
- What are the farmer's and buyer's contract obligations? Are the obligations clear? (3–7)
- What happens if the farmer or the buyer fails to fully perform contract promises? (3–9)
- How can the contract be amended? (3–12)
- Does the contract require exclusivity? (3–13)

### Ground Rules (Ch. 4)

- Does the contract have a disaster clause, and is the disaster clause organic-friendly? (4–1, 4–5)
- Does the contract call for confidentiality? (4–9)
- Must the farmer guarantee the farm product is free of security interests or liens? (4–15)
- Does the contract require insurance? (4–17)
- Does the contract limit the buyer's liability and/or mention "indemnification"? (4–19)

### Duration, Termination & Cure (Ch. 5)

- How long will the contract last? (5–1)
- Can the contract be terminated early? Who can terminate, and for what reason? (5–3)
- What if the buyer goes bankrupt? (5–10)
- Can you fix a broken contract promise? (5–14)

### Price, Quantity & Quality (Ch. 6)

- How is the base price determined? (6–1)
- Is there a clear mechanism for earning premiums and taking discounts? (6–4)
- When will the farmer be paid? (6–6)
- Is quantity set at a specific amount or based on production or acreage? (6–10)
- Can contract quantity be increased or decreased during the contract term? (6–12)
- Does the contract involve cleaning? (6–13)
- Does the contract include a utilization clause or a quota option? (6–18)
- Is quality measured objectively? (6–20)
- If quality testing is required, are test conditions clearly defined? Can the farmer dispute a test result? How? Does the farmer have access to samples after testing? (6–22)
- What are poor quality consequences? (6–27)

**Quick Checklist for Organic Contracts, continued...****Transport, Delivery & Storage (Ch. 7)**

- How does the contract handle transportation, delivery, and storage? (7–1, 7–17, 7–21)
- Are there any packaging requirements? (7–4)
- What kind of documentation is required as part of the organic shipping process? (7–9)
- How does the contract handle contamination prevention during and after transport? (7–12)

**Interaction with NOP Regulations (Ch. 8)**

- How does the contract address organic certification and enforcement? (8–1)
- How does the contract handle pesticide residues and prohibited substances? (8–4)
- How does the contract handle GMOs? (8–5)
- Does the contract set out specific isolation, buffer, or anti-contamination requirements? (8–11)
- Does the contract address access to pasture or the outdoors for livestock or poultry? (8–14)
- How are organic seed rules handled? (8–16)
- Must the farmer plant a particular type of seed, such as buyer-provided seed? (8–18)
- Does the contract place restrictions on the farmer's use of buyer-provided seed, or the resulting crop? (8–20)
- Does the contract give the buyer access to organic records (or certifier records)? (8–24)
- Does the contract address “split operations” or non-organic crops or animals? (8–26)
- Does the contract provide support for transition to organic production? (8–27)

**Beyond Organic (Ch. 9)**

- Does the contract require practices above and beyond NOP regulations? (9–1)
- Must the farmer satisfy marketing claims in addition to certified organic? (9–3)
- Must the farm look “pleasing”? (9–5)
- Are unspecified “best management practices” required? (9–6)
- Can the buyer inspect the farm? (9–7)
- Does the contract incorporate separate buyer-created policies? Or laws? (9–9)
- Does the contract address food safety practices? (9–13)

**Dispute Resolution (Ch. 10)**

- Where will disputes be resolved, and which state's law will apply? (10–1, 10–2)
- Is arbitration required, or can the farmer use the public court system? (10–4)
- Is mediation required? (10–6)
- Will the farmer have to pay the buyer's attorney fees and/or costs if the farmer comes out on the losing end of a dispute? (10–7)

## SEVEN RULES OF CONTRACTING

### 1. **The contract almost always favors the party who wrote it – usually the buyer.**

To the extent that farmers are offered written contracts, these are generally pre-printed contracts written by the buyer (or the buyer's lawyer), with language favorable to the buyer. This means farmers typically begin contract negotiations from a defensive position. Start with the assumption that the proposed contract attempts to place all the risks (financial or otherwise) squarely upon your shoulders. Do not trust that the contract fairly allocates risk, even if you have a good relationship with the buyer.<sup>1</sup> Instead, be sure to read the contract carefully, identify contract language that might cause issues for your operation, and attempt to negotiate more favorable language as necessary. This guide is intended to help you with this process.

### 2. **The buyer can force you to fully perform your contract promises.**

It is very important to understand what the contract obligates you to deliver, because the buyer will likely be able to force you to fulfill that promise or pay for its costs of making up any shortfall. For example, if you contract to deliver 100 bushels of corn to a buyer, but you only deliver 80 bushels, the buyer would likely be entitled to demand you deliver the 20 remaining bushels at the contract price. This can be true even if you have to purchase those 20 bushels on the spot market for much more than your contract price. Alternatively, you could be required to satisfy your contract promises by paying the buyer the amount of money necessary to cover your shortfall at the market price.<sup>2</sup>

Furthermore, be aware that buyers often refuse to pay anything until they receive full delivery under the contract. Although the farmer could go to court and force the buyer to pay for whatever amount was delivered, this can be an expensive and time-consuming process. Plus, even if the court orders the buyer to pay for delivered product, the court would likely subtract the amount required to reimburse the buyer at market prices for the farmer's shortfall.<sup>3</sup>

To minimize the risk of having to pay a buyer for a contract shortfall or having to face the time and expense of a court or arbitration proceeding, it is important to be sure that what you are promising in the contract is



reasonable and that you can manage the risk of low yields or other threats to your expected production.

**3. You cannot assume your failure to perform contract promises will be excused.**

If you are worried about performing certain aspects of the agreement, make sure to talk to the buyer before it is too late to keep your contract promise. Never assume that the buyer will excuse any failure on your part to fulfill your promises under the contract, even if the failure seems insignificant to you. If you talk to the buyer and it agrees to excuse part of your obligations under the contract, make sure to confirm the new agreement in writing. If you don't, any oral agreement you make will likely not be enforceable.

**4. Oral promises made during negotiations or after a contract is signed mean nothing if they are not written into the contract.**

No matter what you and the buyer might have talked about and agreed to in conversations about your agreement, at the end of the day, the only thing that matters is what is written in the contract. This is especially true if your contract includes a “merger clause,” which is a very common provision stating that all parts of the agreement are included in the written contract. Unless contract language is truly unclear, the meaning of the contract is entirely determined by the words contained within the contract.

Example: A proposed contract says, “Buyer will not accept bruised apples.” You have the following conversation with the buyer:

You: “Does that really mean all bruises, including tiny bruises, or does it just mean serious bruising?”

Buyer: “Of course it only means serious bruising. We would never reject your apples if they just have small bruises.”

You: “Oh, okay, sounds good.”

You are reassured by the buyer's statement and sign the contract. If the buyer later rejects your slightly bruised apples, your recollection of the buyer's assurance will not protect you. The contract clearly states that bruised apples will not be accepted, so the oral conversation you had prior to signing likely means nothing.

**Get the buyer's oral explanations in writing**

If a buyer tells you the contract means something even slightly different from what the contract actually says, make absolutely sure to write the true meaning into the contract before signing it. You can hand-write the details right on the pre-printed contract before signing.

**5. Language that sounds “reasonable” or that the buyer describes as “standard” might have hidden consequences.**

Don't ignore contract language that seems like “filler” or that the buyer waves off as “standard language.” Over the course of the contract relationship, these terms can become just as important as price terms. For example, the contract presented to you might include a confidentiality provision stating you cannot share the information in the contract with anyone else. This might sound reasonable at the time, and the buyer might say it is standard policy. However, this provision could turn into a serious problem down the road if it prevents you from seeking legal advice from an attorney or sharing information with your spouse or lender. Therefore, you should read “standard language” just as carefully as the rest of the contract, and think about how it could affect your operation.

**6. Higher price terms might not mean larger payouts.**

Although a premium price for a high-quality or specialty crop might seem attractive, make sure you determine whether you will have to spend more money or take on more risk in order to produce a crop to the buyer's specifications. Will you have to spend more on soil tests, weeding, irrigation, or seed? Will the buyer be extremely strict about quality standards, resulting in rejection of a large percentage of your crop? Make sure to take additional costs and risks into account, lower your profit expectations accordingly, and then evaluate whether the contract is worthwhile.

**7. Contracts are subject to negotiation, and you can walk away.**

Even if the buyer offers you their “standard” written contract, it is perfectly acceptable to ask the buyer to take out terms or to change terms. Don't be afraid to mark up any written contract the buyer offers you. Cross out provisions you don't like, rewrite provisions that are unclear,

and/or write in new provisions. The buyer may not be willing to accept all (or any) of your handwritten changes, but you may be able to negotiate a compromise position.

If the buyer will not negotiate, remember that you can turn down a contract offer. Don't let yourself be pressured into making promises you will regret. On the other hand, recognize that you will never be offered a perfect contract. Examine your other sales options before beginning serious contract negotiations so that you know what your bargaining position is. Have a sense of what types of contract provisions would be deal-breakers and which ones you could accept if the terms are otherwise favorable.

## **BEFORE SIGNING ON THE DOTTED LINE: TEN QUESTIONS**

Although each contracting situation is unique, farmers can achieve fairer contracts by asking and answering the following questions before signing a contract. This process might be tiring, and you might feel self-conscious about taking the time to look so closely at each part of the contract. Or you might be worried about seeming not to trust the buyer. Try not to let these feelings get in your way. Remember, buyers protect themselves by having lawyers draft and review proposed contracts. It is only fair that you have a chance to protect yourself as well.

Taking the time for a truly thorough review and negotiation prior to signing a contract—even if it feels uncomfortable—can help you clarify your relationship with the buyer and avoid serious financial or legal trouble down the road. Additionally, you have the most power just before signing the contract. The buyer needs your production and wants to work with you.

### **1. Have I read every word of the contract?**

The answer to this question must be a resounding, “Yes!” In fact, you might want to read the contract a few times, just to be sure you catch every issue. Beyond representing a serious commitment, the contract terms determine how the risks are divided between you and the buyer.

A smart approach is to ask another person to read the contract, such as your attorney, spouse, or another farmer. Often someone without a connection to the transaction will spot issues in a contract that you might not see. Note that it is often worth investing in legal advice before signing a contract, especially if the contract involves a sizable portion of your production or expected income, a significant investment, or a long-term commitment. Hiring a lawyer to spend a few hours reviewing your contract could save you thousands of dollars down the road.

### **2. Do I understand every single provision of the contract?**

After you have read through the contract a few times, make sure you understand what each provision means for you and your farm. If something goes wrong, what will happen? If anything seems unclear,

make sure to ask questions. If the buyer representative you are working with cannot answer your questions, find someone within the organization who can. When you do get an explanation, try to: (1) negotiate changes if necessary; or (2) have the buyer's more detailed explanation written into the contract. Once again, you should assume that you are bound by the words written into the contract. If any part of the contract is unclear or lacks detail, you are accepting more risk. And don't accept a buyer's spoken assurances that the contract won't be enforced as it is written.

### **3. Is the contract likely to be profitable?**

After deducting the costs of production and any predictable quality deductions from expected payments, are you likely to turn a fair and adequate profit from the contract? Put another way, is the contract likely to benefit you more than selling your product on the spot market?

If you do not have information to help you estimate costs of production for a particular crop, dairy product, or type of livestock, can your local Extension service, Farm Service Agency office, Farm Business Management instructors, other organic farmers, or other organic farming resource organizations help you estimate costs of production?

Make sure to include feed, veterinary services, labor, insurance, tools, supplies, energy costs, organic certification, contamination prevention, quality testing and sampling, product transport, and other costs appropriate to your production in your profitability analysis.

### **4. What happens if something goes wrong?**

One way to think through contract issues is to look at each provision and to imagine that something goes wrong. According to the contract, what happens?

For example, a contract could state that your crop must be free of GMOs. When you make delivery after harvest, an employee of the buyer might conduct a GMO strip test. The result tests positive for GMOs. What happens now? Does your contract provide a mechanism to challenge the result of the GMO strip test, perhaps with a sample you provide or with a laboratory test? Or does the contract say nothing, allowing the buyer to reject your crop without a second test? These are all questions that are best resolved prior to signing the contract.

Examples of common issues under organic contracts include contamination from prohibited pesticides and other substances from neighboring farms, or "drift"; loss of organic certification on all or a

portion of a farm; crop losses due to insect, weed, or disease pressures; and drought, flood, frosts, or other extreme weather events.

Sometimes, silence can be the most dangerous element of a contract. To help make sure your contract covers common issues in organic production and marketing, we have developed a checklist of questions to think about when reviewing organic contracts. See the Quick Checklist for Organic Contracts on pages 2–2 and 2–3 of this chapter.

**5. Would an outsider understand exactly what the contract terms mean? In other words, are the terms clear?**

A proposed contract might include language like, “Grower agrees to allow Buyer continuous access to organic farm records.” This might sound reasonable. But what does the vague term “continuous access” really mean? Does it mean the buyer can access the records at any conceivable time? How about in the middle of the night or on Christmas Eve? How about when you are busy or out of town?

If the organic market price drops below the contract price, a buyer might try to use vague terms like “continuous access” as leverage. This buyer could argue that you breached the contract because you wouldn’t agree to allow records inspection at midnight. Instead of trying to cancel the contract, though, the buyer might say something like, “Well, we will overlook your breach—but only if you agree to sell us your product for less than the contract price.” Having technically violated the strict terms of the contract, you might feel pressured into accepting the lower price.

Clear contract language allows you to understand what the contract really means, and to make an informed decision about whether you want to accept the risk presented by a particular contract provision. Clarity can also help you avoid risks that might be hidden within vague language.

Additionally, if you end up in court, a judge will decide what your contract means. Most judges won’t know you, won’t know how your operation works, and won’t know anything about how the contract was formed. Therefore, you should try to make every part of the contract so clear that an outsider will understand exactly what you meant to agree to when you signed the contract. One strategy to increase clarity is to add a “definitions” section that precisely defines terms used throughout the contract.

**6. Do I have a copy of all parts of the contract, including separate schedules, purchase orders, or buyer policies incorporated by reference? Have I read all of these documents?**

Contracts often consist of a set of different documents. The buyer will not always provide you with all the parts of a contract, so you may have to ask for copies. Further complicating matters, it is not uncommon for provisions in one contract document to contradict provisions in another contract document. To protect yourself, make sure you understand how the different documents interact. Ask the buyer to eliminate any contradictions before you sign any part of the contract.

Additionally, contracts often reference and incorporate outside information or documents. You should insist upon receiving and reading a copy of any law, ordinance, schedule, pay scale, buyer policy, or other document that the contract refers to and makes a part of the contract (this is called “incorporation by reference”). Try to determine how the incorporated document will affect you (see Chapter 9, pages 9–9 through 9–12, for further discussion of incorporated buyer policies and laws).

If you don’t fully understand how particular contract provisions or parts of the contract will affect you, consult an attorney licensed to practice law in your state. Alternatively, ask the buyer to delete problematic provisions from the contract.

**7. Do I have a clear picture of the buyer’s financial situation and reputation?**

Assurance that you will be paid for your production is obviously extremely important. One way to learn about the financial health and/or reliability of buyers is to ask other organic farmers about their dealings with particular buyers. You may discover that farmers have trouble with certain buyers but recommend others. This kind of information is invaluable and should influence your contracting decisions. You may be better able to get information about buyers’ reputations, as well as pricing information, by joining a cooperative marketing association or some other type of farmer association.

Keep in mind that if a buyer goes bankrupt after taking possession of your crop, you may become the buyer’s unsecured creditor and have difficulty getting paid. This is one reason why it is important to know about the financial stability of your buyers and to demand prompt payment. See Chapter 12 for more information about how producers may be able to protect themselves from losses that can occur when a buyer files for relief in bankruptcy.

## **8. What happens if a contract dispute arises?**

It is important to know what the contract says will happen if a dispute arises between you and the buyer. Many buyers offer contracts that include language stating you will agree to arbitrate any disputes that arise during contract performance. If you agree to arbitration, you give up the right to your day in court. This is a big deal, because arbitration is often much more expensive than a court action—often prohibitively expensive. Also, even if you would never have considered going to court against a buyer, the mere fact that you *could* file suit could give you leverage in negotiations with the buyer, leverage that is lost under a requirement to arbitrate. (See Chapter 10, pages 10–4 through 10–6, and Chapter 12, page 12–5, for more information on arbitration.)

In addition, does the contract say anything about which laws or courts will govern disputes that arise? If you live in Florida and the contract states that disputes will be resolved in a Wisconsin state court according to Delaware laws, you will be at a significant disadvantage in any lawsuit. Try to negotiate terms allowing for disputes to be decided in a court near you under the laws of your state. That way, if you end up in court, you won't have to pay expensive travel costs, and it will be easier to find a local lawyer familiar with the applicable laws.

## **9. Have I attempted to negotiate the contract, and have all negotiated changes been put in writing?**

If you are handed a pre-printed contract and you want any provisions added, clarified, deleted, or otherwise changed, be sure to: (1) ask for what you want; and (2) make sure the changes are made in writing.

The contract negotiation process is your best opportunity to identify and resolve misunderstandings before entering into a legally binding agreement. Thorough negotiation might also help you avoid a bad deal. Don't sign the contract until everything has been changed to your satisfaction. In a best case scenario, the contract should reflect a fair allocation of risks and rewards between you and the buyer.

## **10. Taken together, are the negotiated contract obligations and associated risks worth my time, hard work, and financial investment?**

If your contract relationship with the buyer is unsuccessful, you risk losing your financial investment in the organic product and your effort to produce the product. You could also face attorney fees and court or arbitration costs if the buyer sues you or you are forced to sue the buyer



for payment. Finally, you could face legal penalties if the buyer successfully argues that it was harmed by your failure to carry out your promises under the contract. Having made your best effort to get the contract language as clear and even-handed as possible, are you satisfied that the risks of failure and your exposure in case of failure are at acceptable levels? Keep in mind that no matter what particular pressures persuade you to sign a contract (financial, family, or otherwise), you cannot later be excused from your commitment by claiming personal circumstances forced you to sign a contract against your will. Whether it is true or not, the law assumes that you are always free to walk away from a buyer's contract offer.

## **CONTRACT NEGOTIATION STRATEGIES**

### **Do your homework**

Preparation is the key to successful negotiation. Talk to other farmers. Research the market for your particular organic commodity, and try to find out what typical contracts look like. To this end, consider joining together with other farmers to form a marketing association. Also, spend some time thinking through what kind of contract terms you are willing to agree to, and what kind of terms you will not accept. Analyze your needs, concerns, goals, and fears. Define what is most important to you, and think about whether other marketing opportunities exist that could satisfy your interests as well as the offered contract. Knowing how you define success and what you will do if you don't reach an agreement can prepare you to walk away if the proposed contract does not meet your needs.<sup>4</sup>

Because buyers often want a quick agreement, consider asking a lawyer, accountant, or other trusted adviser to be available during the negotiation timeframe (either in person or by phone). The viewpoint of someone you trust who is not personally involved in the arrangement can be invaluable during time-pressured negotiations.

Also, at the outset of negotiations, consider offering your own proposed contract, an amended version of the contract being offered, or at least a list of essential terms that you want included (or not included) in the final agreement. Negotiating from your own contract can provide you with a better bargaining position. Your contract does not have to be long or complex.

### **Use a cheat sheet**

It is easy to lose your way in the heat of negotiation. Ensure you address all of the issues you are concerned about by using a checklist (see the Quick Checklist for Organic Contracts, pages 2–2 and 2–3 of this chapter) or other detailed notes. To ensure you don't miss anything, bring a list of questions to ask, terms to watch out for, provisions you want to make sure are in the contract, etc. You could even bring this guide, or a part of this guide.

**Easy, Effective Negotiating Tip**

Bring an ally to the negotiating table (for example, a spouse, friend, relative, or lawyer). That person can provide invaluable moral support, even if they are just there to observe. An ally can also help you buy time to think, because you can ask the buyer to let you and your ally “take a moment” for a private discussion. You can use that private time to gather your thoughts and refocus on your negotiating strategy.

**Mental and physical preparation**

Be mentally prepared for the negotiation itself. If you expect intimidation, peer pressure, fear, or “take-it-or-leave-it” contract offers, you can craft a coping mechanism prior to entering negotiations. It can also be helpful to have a phrase in mind to use when you need to politely say, “No way.” One example is, “I’m not really comfortable with that provision.” Or, “I’d feel better if we added something about [insert topic here].”

If you are conducting face-to-face negotiations, prepare for the awkward feeling that comes with reading every word of a proposed contract under a buyer’s watchful eye. To avoid this issue, you could ask for some time to consider the contract in a more private space.

Physical preparation is also important. Don’t go into a contract negotiation tired or hungry. You need physical stamina to push through tiring negotiations.

**During the negotiation****Take Your Time**

Tell the buyer you need at least a few days to consider the contract offer. If they refuse, you can still be prepared for a quick decision if you have followed the advice outlined above. However, if the buyer agrees, you are in a much better position. You now have time to thoroughly evaluate the contract, including estimating the costs of everything the contract requires. You also have the opportunity to search out and compare other marketing options.

If you must decide whether to sign the contract during the first negotiating session, you can buy yourself some time by asking for breaks

to privately discuss the contract with someone else (a lender, spouse, business partner, or anyone you choose), either by phone or in person. Even a bathroom break could allow you time to privately gather your thoughts.

#### Ask Questions, and Be a Firm Negotiator

Above all, be sure you thoroughly understand every provision in every document included in the contract before signing anything. Ask questions if anything seems unclear.

#### Remember That You Have (Some) Bargaining Power

Even if you, as a farmer, may have less power than buyers in some respects, remember that you do have some leverage. Buyers contract with farmers because they need your production to stay in business. Buyers also depend upon contracts for quality control, securing adequate supplies of scarce resources, stabilizing input prices, lowering procurement costs, and managing risks.<sup>5</sup> As a result, especially if you are a reliable supplier of certain high-quality, in-demand organic commodities (for example, organic grains), you likely have some bargaining power.<sup>6</sup>

However, if you are a seller in an over-supplied market (for example, a dairy farmer during 2008-2009), you may not have much bargaining power. In either case, joining together with other farmers in some type of collective organization—like a marketing association or a collective bargaining cooperative—may help you gain bargaining power and better contract terms.

## **AFTER YOU SIGN**

### **Communicate with the buyer**

A contract is just the beginning of a longer relationship. The best thing you can do to avoid contract problems during the course of your relationship (besides having a clearly written contract) is to communicate regularly with the buyer.

Communication is especially important if you anticipate you will not be able to keep your contract promises. The buyer may agree to alter your agreement to accommodate your new circumstances. Again, remember that contract modifications are legally ineffective unless they are in writing. Send the buyer a letter confirming any contract modification.

### **Keep records of everything related to the contract relationship**

Records are like insurance—you may never need them, but if a problem arises, you will be glad to have them. Keep copies of documents like invoices, packing lists, delivery logs, bills of lading, weight tickets, and payments. Write down the date they were signed, sent, or received. Since many buyers pay for organic commodities only after they have received an invoice, make sure to send invoices right away.

Also, keep written notes of any phone conversations with the buyer. This is particularly important if you reach an agreement over the phone that changes requirements for contract performance. Often, disputes arise simply because the parties forgot the exact details of their spoken arrangement.

It is a good practice after every significant conversation with the buyer, including phone conversations, to write the buyer a letter describing all oral agreements reached and other important points from the conversation as you understand them. Ask the buyer to respond in writing within 10 days if the buyer disagrees with anything you describe in the letter. Keep a copy of the letter for yourself, and send a copy to the buyer by certified mail, return receipt requested. Save your receipt showing that the buyer received the letter. These kinds of records protect you because you can point to the letter as evidence of the agreement.

See Chapter 12 for information about solving problems that commonly arise during contract relationships.

## CHAPTER 2 — ENDNOTES

- <sup>1</sup> Adapted in part from Neil D. Hamilton, *The Legal Guide for Direct Farm Marketing*, Drake University Agricultural Law Center, at 72-74 (June 1999) (Ten Rules of Contracting for Direct Farm Marketing).
- <sup>2</sup> See, for example, *Melford Olsen Honey, Inc. v. Adee*, 452 F.3d 956 (8th Cir. 2006) (farmer failed to deliver all honey due under the contract).
- <sup>3</sup> See, for example, *Melford Olsen Honey, Inc. v. Adee*, 452 F.3d 956 (8th Cir. 2006) (farmer failed to deliver all honey due under the contract; buyer ordered to pay for honey delivered but farmer ordered to pay buyer's damages for procuring remaining honey at a higher market price).
- <sup>4</sup> Stephen Frenkel, *Power Differentials in Negotiation: Don't Let 'em Push You Around*, Harvard Negotiation Law Review (October 21, 2009), available at <http://www.hnlr.org/?p=441>.
- <sup>5</sup> Carolyn Dimitri, Lydia Oberholtzer, and Michelle Wittenberger, *The Role of Contracts in the Organic Supply Chain: 2004 and 2007*, EIB-69 at 10-11, U.S. Department of Agriculture, Economic Research Service (December 2010).
- <sup>6</sup> Carolyn Dimitri, Lydia Oberholtzer, and Michelle Wittenberger, *The Role of Contracts in the Organic Supply Chain: 2004 and 2007*, EIB-69 at 1, U.S. Department of Agriculture, Economic Research Service (December 2010). See also Stephen Frenkel, *Power Differentials in Negotiation: Don't Let 'em Push You Around*, Harvard Negotiation Law Review (October 21, 2009), available at <http://www.hnlr.org/?p=441>.

# 3

## Parties & Contract Relationship

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### CHAPTER QUICK TIPS

#### **Confirm Contract Changes in Writing**

Valid contract changes should be in writing. Send the buyer a letter confirming the details of the change you have agreed to, and asking the buyer to respond promptly if the buyer does not agree with the details as written.

#### **Get Lender Input Before Signing**

If you bring a contract offer to your lender prior to signing, you can negotiate with the buyer to incorporate any lender requirements – helping avoid issues with obtaining credit to cover input costs.





## **THE PARTIES**

### **Who are the parties to the contract?**

In most organic contracts, there will be only two parties:

- (1) you, the farmer and “seller”; and
- (2) the buyer, which could be an individual, marketing cooperative, processor, broker, distributor, restaurant, or other entity.

Even if there are only two parties involved, it is usually a good idea to double-check that the parties are listed accurately in the contract. It is not uncommon for buyers to use the same contract template to contract with multiple farmers, so make sure your name or your farm business name appear correctly throughout the contract. Also, if you have a farm business name, it is generally best to use that name on the contract—either instead of or in addition to your name.

### **Dealing with Buyer Subsidiaries**

If you are considering a contract with a corporate buyer, it’s a good idea to check whether the buyer named in the contract is the company you expected to do business with, or whether the named buyer is actually a subsidiary of that company. In some states, if the named buyer is a subsidiary, the larger parent company may not be responsible for the debts or other liabilities of the subsidiary.

If you are unexpectedly confronted with a subsidiary as the named buyer in your contract, you may wish to do one or more of the following:

- Ask that the larger parent company be substituted or added as a party to your contract.
- Include contract language stating the parent company is liable to you for any of the subsidiary's debts.
- Consult with an attorney about the corporate liability laws in your state. Some states have laws that prevent companies from using subsidiaries to protect themselves from liability.



### **Who owns the organic farm product being sold – the buyer or the farmer?**

As discussed in Chapter 1, if the relationship described in your contract makes it clear that the farmer owns the organic product throughout the production cycle, your contract is a marketing contract. Marketing contracts describe sales of goods (for example, organic crops, dairy or livestock). A certain set of laws, including laws based on Article 2 of the Uniform Commercial Code (U.C.C.), apply to contracts for the sale of goods. Many of these laws are discussed in Chapter 1 and Chapter 12.

If, on the other hand, a contract makes it clear that the buyer—not the farmer—owns the organic product throughout the production cycle, the contract is a production contract. Generally, production contracts describe the sale of services (for example, caring for organic crops or livestock), not the sale of goods. A different set of laws applies to contracts for the sale of services. Additionally, some state and federal laws apply specifically to production contracts for the sale of agricultural services. As stated in Chapter 1, this guide is focused on marketing contracts for the sale of goods—not production contracts for the sale of services. If you are considering an organic production contract, consult an attorney licensed to practice law in your state to understand your risks and what legal protections are available.<sup>1</sup>

**Flock-to-Flock Production Contracts:  
A Longstanding Problem**

Production contracts have wreaked havoc on the farm finances of conventional poultry and livestock farmers for many years. One of the worst examples of production contract arrangements are the “flock-to-flock” broiler contracts routinely offered to poultry farmers. This type of contract typically involves a corporate poultry processor (for example, Tyson or Perdue) offering a contract that requires a farmer to build poultry houses to the processor’s specifications. These commonly cost \$200,000 or more per house. In return, the farmer is paid for the services required to produce the processor-owned broilers. However, these contracts are only offered on a “flock-to-flock” basis, meaning that the contracts only last for the duration of one broiler flock—typically six to eight weeks. Although the contracts provide for—and farmers are counting on—open-ended renewals, there is never a guarantee. The problem comes when the processor decides to terminate a flock-to-flock contract relationship before the farmer can recover the substantial investment on the poultry houses. The end result is often financial ruin.

Although organic poultry production contracts are still relatively rare, farmers considering organic poultry production would be wise to steer clear of production contracts.

**Is anyone else’s approval required before the contract can begin?**

It is not uncommon for a contract to require the approval of someone else—like a lender, a landlord, or a spouse—before the contract can become effective. These so-called “third parties” are not directly involved in the contract but have a close connection to one or both of the contracting parties and generally have something at stake in their operations, often either as a partner or creditor. If such approval is required, make sure to obtain it before taking any significant steps that rely on the contract working out, like purchasing seed, feed, or other

inputs. If approval by a third party does not seem appropriate in your situation, consider asking the buyer to delete that requirement.

**Include Lenders Early in Organic Contract Negotiations**

It is not uncommon for a lender to require a farmer to provide a marketing contract as evidence that the farmer will be able to make payments on a line of credit, mortgage, input lien, or other type of credit arrangement.

Some lenders may not understand organic production, or may be biased against organic farming due in part to the mistaken belief that organic farming is more risky than conventional farming. Lenders that are wary of lending to organic farmers may be concerned about specific contract provisions, like whether the organic pay price for milk will increase if feed prices increase.

Rather than bringing your lender a finalized contract that cannot easily be changed, consider bringing your lender a contract offer prior to signing. That way, you can negotiate with the buyer to incorporate any changes the lender requires. Also, you will be less likely to breach your contract because you cannot fund the input costs required to fulfill your organic contract. Additionally, you may be able to use the lender's requirements as leverage to negotiate a better deal with the buyer.





A requirement for third-party approval of an organic contract could come up if the farmer is required to provide proof of organic certification prior to the contract taking effect. The certification itself, of course, requires a qualified organic certifier (a third party) to issue the certification. If your organic contract requires organic certification prior to the contract taking effect (not just prior to beginning production), be sure to settle the certification issue promptly because neither party is bound to the contract until you obtain certification.

If you have a provision requiring certification prior to the contract taking effect, be sure to keep a record of the date you obtained the certification so that you have proof the contract has begun. It would also be prudent in such cases to notify the buyer in writing of the date you obtained the certification.

### **Does any part of the contract describe you as a merchant?**

If any part of the contract describes you as a “merchant,” the contract is making clear that you are a person who can legally be considered to have a good understanding of the business aspects related to the organic farm product you are selling. A merchant is defined as “a person who deals in goods of the kind or otherwise by his occupation holds himself out as having knowledge or skill peculiar to the practices or goods involved in the transaction.”<sup>2</sup> In other words, merchants are businesspeople who are knowledgeable about their particular business. As a result of this level of knowledge, contract law generally holds merchants to stricter standards than non-merchants and removes some of the formal requirements for sales agreements to make it easier for merchants to quickly make deals, assuming that they are knowledgeable enough about the risks to protect their own interests.

#### **You and the Buyer Are Probably Merchants**

Farmers who regularly sell organic farm products should know that they probably qualify as merchants in organic farm products regardless of what the contract says.

Courts often consider farmers to be merchants if they regularly sell crops and/or livestock.<sup>3</sup> Therefore, it is usually safest to assume that you would qualify as a merchant and to operate according to the more rigorous contract laws that apply to merchants (like the implied warranty of merchantability, discussed on the next page, and the contract formation rules discussed in Chapter 1, pages 1–2 and 1–3). Any buyer who regularly

deals in organic farm products is probably going to be considered a merchant as well.

Even if your contract says you are a merchant, or is silent about whether you are one, there is a small chance a court might later decide that you are not a merchant. Courts have looked closely at the particular facts of each case to decide whether or not a farmer is a merchant.<sup>4</sup> If you are considered to be a non-merchant, some parts of contract law treat you more leniently because they assume you are not a businessperson. Also, some contract formation rules may not apply if you are not a merchant; this could make it more difficult for you to form an enforceable contract with an informal writing (like a purchase order).

Again, though, most farmers and almost all buyers will qualify as merchants under contract law.

#### Implied Warranty of Merchantability

Part of the stricter standards that contract law imposes on merchants is the “implied warranty of merchantability” that often applies when a merchant sells goods. An implied warranty of merchantability is a promise that the goods will conform to the description in the contract and will be of adequate quality. The warranty is “implied” because it exists even if the contract itself says nothing about a warranty of merchantability.

It is possible for a contract to successfully disclaim a warranty of merchantability by specifically stating in the contract that this kind of warranty does not apply. Still, it is unlikely any organic buyer would accept this kind of disclaimer in a contract for organic farm products because quality and organic integrity are highly valued in the organic marketplace.

## THE CONTRACT RELATIONSHIP

The contract provisions discussed in this section describe the nature of the business relationship between organic farmers and buyers.

### **Are the buyer’s contract obligations clear?**

Generally, the buyer’s main obligations are: (1) to accept delivery of the organic commodity under contract; and (2) to make appropriate and timely payments. However, organic contracts vary widely, and buyers may take on additional obligations. For example, buyers might provide inputs or training, agree to market the organic commodity on the farmer’s behalf (especially if the buyer is a marketing organization), or provide support for the farmer’s organic transition and/or certification. Buyers might also cover transportation costs, or agree to certain dispute resolution procedures.

What is most important is identifying and understanding what the buyer is and is not obligated to do. If necessary, consider changing the contract language so that the buyer’s obligations are clear. Be aware that the buyer’s contract obligations may be found in multiple sections scattered throughout the contract.

### **Are the farmer’s contract obligations clear?**

Identifying and understanding your contract obligations is also extremely important. Like the buyer’s obligations, your obligations may be scattered throughout the contract—even under contract headings that seem unrelated to your contract duties. Try to assess whether the contract obligations will outweigh your expected benefits under the contract.

Because contracts are often presented to farmers on a “take it or leave it” basis, and the extent to which buyers are willing to negotiate on specific contracts varies widely, it is wise for farmers considering a contract offer to first determine whether the contract is a deal worth signing as written. The information contained in this guide can help you make that decision, and identify areas for possible improvement through negotiation. Later, if your negotiation attempts are rejected, you will have already made an informed decision about whether you are willing to accept the contract as-is, and you will be able to give the buyer an informed response to the contract offer.

When thinking about potential areas of improvement through negotiation, remember that both farmers and buyers can benefit from making vague or unclear contract language clearer. When the parties expect different results from the same contract, contract disputes are common. Both sides benefit when clarity prevents expensive and unnecessary disagreements.

**Example: Vague Provision**

Seller agrees to use best management practices in performing all aspects of the instant agreement.

It is unclear here what “best management practices” really means. Vague provisions like this one give farmers an opportunity to begin discussions with buyers about what kind of practices are expected. You may discover that vague language is unnecessary and can easily be deleted. Or, when you have clarified what the buyer really means by “best management practices” (or by another vague provision), you can write the clarifying details into the contract.



**Better Example: Vague Provision Clarified**

Best Management Practices: In performing all aspects of this contract, Buyer and Seller agree that Seller will comply with the federal organic regulations (the NOP regulations).

Unlike the example in the box above, this language clearly states that “best management practices” equals compliance with NOP regulations.



The types of organic contract obligations discussed throughout this guide can appear in an organic contract in unlimited varieties and combinations. You can use the guide to help you understand your contract obligations and the potential implications of those obligations.



### **Breach: What happens if the farmer or the buyer fails to fully perform or keep contract promises?**

Failing to keep a contract promise is called “breach.” Generally speaking, if one party breaches the contract, that party will suffer some type of consequence under the contract. Common consequences for breach include: termination of the contract, rejection of goods, and reduced payment.

#### Farmer Breach

Organic contracts often discuss what will happen if the farmer fails to keep contract promises. Some contracts will include specific consequences tied to specific breaches (for example, if you breach the contract by delivering late, the consequence could be a \$100 penalty for each day you are late). Other contracts will include a so-called “blanket breach provision” (discussed further in Chapter 5, pages 5–4 through 5–7) that spells out what would happen if you failed to comply with any provision of the contract (for example, if you commit any breach no matter how minor, the buyer can cancel the contract). Some organic contracts include both specific and blanket breach provisions.



#### Example: Blanket Breach Provision

Breach of Contract: Seller agrees to comply with all terms and conditions herein. If Seller fails to comply with this agreement in any respect, Buyer may immediately declare this contract null and void upon written notice.

Note that this provision is extremely one-sided in favor of the buyer. Only the buyer is given termination power, and only the farmer must promise perfect compliance, with threat of termination for a breach “in any respect.”

Be especially cautious about blanket breach provisions. If something changes for the buyer (the buyer loses a big contract, organic premiums shrink unexpectedly, etc.), and the buyer is looking for a way to get out of the contract, one of the easiest things for the buyer to do is wait for you to make a small misstep and then claim its termination rights under a blanket breach provision.

If You Encounter a Blanket Breach Provision:

- Replace it with a provision that allows termination only for material breach—not for minor breaches. See Chapter 5 for a discussion of material breach.
- If you cannot replace the term with a material breach term:  
Try to get the blanket breach term deleted.

Better Example: Termination Upon Material Breach Provision

Breach of Contract: The parties agree to comply with all terms and conditions herein. If either party commits a serious and material breach of the contract, the non-breaching party may declare this contract null and void upon written notice.



You should also be sure to understand the possible consequences of failing to keep a contract promise, and think about how you would cope if you had to deal with those consequences. If the potential consequences of a breach seem too damaging or risky, think about negotiating less burdensome breach provisions. Consequences of a breach can vary widely, ranging from termination of the contract to payment reduction, rejection of delivery, etc. In the end, if the buyer is requiring consequences for breach that would be too burdensome, consider negotiating new language or finding a different buyer.

Fill the Silence on Farmer Breach

If the contract does NOT state what will happen if one side breaks a contract promise, think about whether you would like to clarify what should happen. Spelling out the consequences of a breach can help avoid a dispute between you and the buyer after a breach occurs. For example, if the contract is silent as to what happens if you deliver product that falls below quality standards, the buyer could decide the appropriate consequence for low-quality delivery is rejection of your entire shipment. In contrast, if the contract states the consequence of low-quality delivery is a 15 percent price discount (not rejection), you are much less likely to lose the entire benefit of your contract and be forced to look for another buyer.

Making the consequences of a contract breach clear can help provide some certainty in case of a breach and help prevent a dispute that could end up in court. Negotiating acceptable consequences in advance can also prevent the buyer from choosing the worst possible consequence if it turns out you cannot keep your contract promises.



When reviewing an organic contract, think through the most likely ways you might be unable to carry out the contract promises. Then figure out whether the contract states what should or will happen if any of those possible breach scenarios occur. If the contract is silent (or unclear), think about negotiating language that spells out what should happen.

### Buyer Breach

Organic contracts are less likely to spell out consequences of buyer breach, perhaps because they are usually drafted by the buyer. Nevertheless, it can be somewhat risky for organic farmers to enter into a contract that is relatively consequence-free for the buyer. Stated consequences for breach can be a powerful incentive for both parties to fully perform their contract obligations. Therefore, consider negotiating consequences for the buyer's breach of its important promises in the contract. For example, if a buyer promises to send payment by a certain date, the contract could impose penalties for late payment.



#### Example: Penalty for Late Payment Provision

Seller shall receive payment within 10 business days of delivery. If Buyer fails to pay by said date, Buyer agrees to pay Seller 1 percent of the contract price for every calendar day payment is late.

### **How can contract terms be changed after the contract is signed?**

Any changes to a written contract should be made in writing. Any changes you do not put in writing will generally not be enforceable in court, even if

the contract says otherwise. See Chapter 1 for a more detailed discussion about forming enforceable contracts.

Many organic contracts will expressly state that the contract cannot be changed except in writing. Some will also require the written amendment to be signed by both parties.

**Example: Modification Only in Writing Provision**

Except as otherwise specified in other provisions of this agreement, the agreement may not be modified or amended except by an instrument in writing signed by both parties.



You should carefully follow the directions set out in the contract for making changes to the contract. At the very least, put everything in writing. Do not rely on promises the buyer makes over the phone or even in person; the contract itself will be unaffected if nothing is in writing. See additional guidance on oral agreements in Chapter 1.

**Send the Buyer a Written Confirmation of Any Contract Changes**

If you and the buyer agree to make a change in the contract terms after the contract has begun, you **MUST** get the change in writing.

An easy way to do this is to send the buyer a letter, fax, or email confirming the details of the change. Include the date of the call or conversation in which you and the buyer agreed to change the terms, and explain all of the details of the new agreement. Make sure to keep copies of all papers related to contract changes.





**Include Provision Stating Contract Can Be Mutually Re-Negotiated During Contract Term**

Mutual re-negotiation is always legally allowed if both parties to a contract agree to change the contract language. However, having a contract provision expressly stating that mutual re-negotiation is allowed can increase the chances that the buyer will actually agree to re-negotiate the contract if needed. At the very least, having mutual re-negotiation language in the contract should prevent a needless dispute about whether the contract can be re-negotiated during the contract term, hopefully focusing the discussion on the pros and cons of changing the contract language.

**Does the contract require exclusivity?**

**Farmer Agrees to Sell Exclusively to the Buyer**

Does the contract require you to sell a particular organic commodity only to the buyer? If so:

- Make sure that the contract includes a reciprocal requirement for the buyer to purchase the entirety of your exclusively produced commodity.
- Make sure that the contract clearly states which organic commodity you are agreeing to sell only to the buyer.
- Make sure that an alternative arrangement exists if the buyer decides for any reason to reject your organic commodity produced for the buyer. You do not want to end up in a situation where the buyer refuses to pay the full contract price and/or rejects your delivery and you cannot sell the product to another purchaser without violating the contract.
- Consider negotiating for a provision that will allow you to sell your product elsewhere (or use your product yourself, like using excess milk to spread on fields) if the buyer rejects your product or refuses to make appropriate payment under the contract.

**Example: Exclusivity Provision**

Seller agrees to provide all organic soybeans produced by Organic Farm to Buyer. Seller further agrees Buyer shall be the exclusive purchaser of Seller's organic soybeans for duration of this agreement.

This provision requires the farmer to sell all organic soybeans produced to the buyer, but does not require the buyer to purchase all of the farmer's soybean production. This could lead to a situation where the buyer refuses to purchase some of the soybeans, but prevents the farmer from selling the rejected soybeans elsewhere.



Adding the following language to the example above would require the Buyer to purchase all of the farmer's soybean production:

Buyer agrees to accept and pay for the entirety of Seller's organic soybean production during the contract term, provided it meets quality standards set forth herein.



Adding the following language to the example on the previous page could protect against a situation in which the Buyer refuses to purchase all of the soybeans the farmer produces, or rejects some portion of the delivery for any reason:

If Buyer refuses to purchase any amount of Seller's organic soybeans for any reason, Seller shall be free to find another purchaser for any soybeans Buyer refuses to purchase.



### Buyer Agrees to Buy Exclusively From Farmer


An exclusivity arrangement can also bind the buyer. For example, the buyer could agree that you are the buyer's exclusive supplier of organic barley for a certain period of time, which would prohibit the buyer from buying organic barley from another farmer for that time period. Generally, buyers would agree to this only if they were confident that one organic farmer could supply all of their product needs.

### **Does the contract state that you are an independent contractor?**

Contracts often state that the parties do not have an employee-employer relationship, that one party is not an "agent" of the other party, or that the parties are not "joint venturers." Sometimes, the contract simply states that one party (probably the farmer in an organic contract) is an "independent contractor." The contract might also state that you and the buyer have a "vendor/vendee" (buyer/seller) relationship.

Under a typical organic marketing contract, these statements will generally accurately describe the farmer-buyer relationship. Thus, as a farmer reviewing an organic marketing contract, agreeing that you are an independent contractor (or a vendee) should not be worrisome. As a seller of goods, you are very unlikely to be an employee or agent of the buyer.

#### Example: Relationship of Parties Provision



NO AGENCY, RELATIONSHIP: The parties to this contract intend to establish a vendor/vendee relationship. Seller is not an agent of Buyer, and neither party is authorized by this contract to act on behalf of the other party. This contract does not form a partnership, licensor/licensee relationship, landlord/tenant relationship, joint venture relationship, employer/employee relationship, or profit-sharing arrangement.

Buyers put these provisions into contracts out of an abundance of caution to easily defeat any arguments about: (1) potential liability, and (2) obligations imposed on employers by federal and state labor laws.

With respect to liability, most states have laws that require an employer to be liable for the acts of his or her employees or agents. This is often termed “vicarious liability.” Therefore, by stating that the farmer is an independent contractor and not an employee or an agent, the buyer is creating evidence to counter any arguments about liability under these laws. Additionally, employment laws create various requirements for employers, such as providing workers’ compensation insurance and unemployment benefits, and collecting payroll taxes. By making it clear that the farmer is not an employee of the buyer, the buyer can protect itself against government enforcement actions or later claims for employee benefits on behalf of the farmer.

**Example: Avoiding Vicarious Liability Provision**

Buyer is not liable for the acts or omissions of Seller; Seller is in all respects an independent contractor and shall not act as Buyer’s agent.



The question of whether someone is an independent contractor or an employee is not determined by contract language alone. Instead, it is a multi-factor test that takes the actual circumstances of the relationship into account.<sup>5</sup> Nevertheless, putting this kind of language in a contract is one way that a buyer could attempt to prove to a court that a farmer is an independent contractor.



**CHAPTER 3 – ENDNOTES**

- <sup>1</sup> See generally Susan E. Stokes, *The Dilemma of Contracting: Risk Management or Risky Business?* (Farmers' Legal Action Group, 2006), available at [http://flaginc.org/topics/pubs/arts/CLE\\_SES.pdf](http://flaginc.org/topics/pubs/arts/CLE_SES.pdf). See also David Moeller, *Livestock Production Contracts: Risks for Family Farmers* (Farmers' Legal Action Group, 2003), available at <http://flaginc.org/topics/pubs/arts/artcfo05.pdf>.
- <sup>2</sup> U.C.C. § 2-104(1) (1977).
- <sup>3</sup> See, for example, *In re Montagne*, 431 B.R. 94, 113 (Bankr. D. Vt. 2010) (determining a dairy farmer is a merchant in all aspects of his mercantile capacity, that is, with respect to goods for dairy farming operations, but not for every purchase of goods).
- <sup>4</sup> See 10 Williston on Contracts § 29:25 (4th ed.), at footnote 9 (May 2012) (“[T]he issue of whether a particular farmer may also be classified as “merchant” within the meaning of U.C.C. § 2-104(1) must be determined on a case by case basis. The court in each case must determine, on the basis of the evidence presented, whether an individual who is considered a farmer also possesses expertise in the area of marketing...sufficient enough to classify him as a “merchant” within the purview of the Uniform Commercial Code.”).
- <sup>5</sup> See *S.G. Borello & Sons, Inc. v. Dept. of Industrial Relations*, 48 Cal.3d 341 (1989) (using a multi-factor test to determine “sharefarmer” cucumber harvesters are employees).



# 4

## Contract Ground Rules

- [4-1](#) What happens if disaster strikes?
- [4-5](#) Is your disaster clause organic-friendly?
- [4-9](#) Does the contract require any level of confidentiality?
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### CHAPTER QUICK TIPS

#### **Confidentiality Applies After Signing**

Confidentiality provisions in a contract do not apply until after the contract takes effect. You are generally free to show a contract containing a confidentiality requirement to an attorney and/or other advisors before signing.

#### **Communicate In Writing**

Even if the contract does not require communication with the buyer to be in writing, you should still communicate important contract-related information in writing. It is also a smart practice to write a short letter or email to the buyer restating any important information the buyer communicates to you in a meeting or over the phone. In the letter, ask the buyer to respond promptly if it does not agree with your restatement of the information.



## **CONTRACT GROUND RULES**

The contract provisions described in this chapter create the ground rules for the farmer/buyer contract relationship.

### **What happens if disaster strikes?**

Does the contract have a clause excusing you (and/or the buyer) from carrying out the contract provisions if a disaster occurs? Such a clause may be labeled “Disaster,” or may be labeled with disaster “code words” such as “Force Majeure,” “Commercial Impracticability,” or “Acts of God.” These disaster clauses usually allow the parties to cancel or modify the contract if conditions occur that make contract performance difficult or impossible. Commonly covered disaster conditions include events like extreme weather events (for example, flood, hail, or excessive heat) and national emergencies.

#### **Add a Disaster Clause If You Don’t See One**

Because extreme weather conditions can have a devastating effect on crop, dairy, and livestock production and your ability to fulfill contract requirements, you should seriously consider adding a disaster clause to your contract if it does not already have one. See the organic-friendly disaster clause recommendations and example on pages 4–8 and 4–9 of this chapter, respectively.

#### **No Protection From Market Changes**

Keep in mind that disaster clauses generally do not protect farmers or buyers from market fluctuations. Unless the contract explicitly states otherwise, you will not be excused from contract performance if the market price skyrockets and you are locked into a low contract price.

Example: Standard Disaster Clause

Force Majeure: If the performance of the party suffering a disaster as described herein is delayed for more than 60 days and/or is substantially impaired, either party may cancel the contract upon written notice. Neither party shall be liable for damages due to delay or failure to perform any obligation under this Agreement if such delay or failure results directly or indirectly from acts of war, civil commotion, riots, strikes, lockouts, interference in telephone communications, carrier delays, fire, flood, windstorms, or other extreme weather events or acts of God, delay or failure to receive raw materials, or any cause of a like or different kind beyond the reasonable control of either party.



The standard disaster clause example above allows for cancellation of the contract after a 60-day delay or if one party's performance is substantially impaired due to one of the listed disasters. To trigger cancellation, the only requirement is some type of written notice to the other party.

In contrast, many organic contracts include disaster clauses that require the farmer to take some actions in addition to written notice before the farmer can take advantage of the protection offered by the disaster clause.

- *Attempt to Minimize Disaster Effects May Be Required*

Your disaster clause might require you, if feasible, to make some sort of effort to overcome a disaster situation and perform under the contract. This could include delivering the portion of your production that was not harmed by the disaster. For example, if half your contracted crop suffered hail damage, you could still be required to deliver the other half of the crop if you retain harvest and delivery capabilities.

You could also be required to provide evidence that you attempted to minimize disaster losses but were unable to do so. If you have this kind of requirement, make sure you take the necessary steps required to respond to the disaster or to show

that the disaster cannot be overcome. You may also wish to delete or modify this requirement before signing the contract if it seems like it could be too burdensome.



Example: Attempt to Minimize Disaster Effects Required

The party suffering disaster damage shall be excused from contract obligations only after providing proof of reasonable efforts to avoid or remove impediments to performance.

- *Immediate Written Notice to Buyer May Be Required*

Some contracts require written notification or evidence of a disaster before you can take advantage of disaster clause protections. You might be required to provide this notification to the buyer within a specific time frame. Failure to provide the notification within the time frame could result in waiver of your right to the benefit of the disaster clause.

If your contract contains a time-sensitive disaster notification requirement, consider whether you feel the stated time frame would be reasonable in the case of a serious disaster situation. In the worst of disasters (for example, a Hurricane Katrina event or a tornado like the one that hit Joplin, Missouri in 2011), it might be impossible to provide notice to the buyer within a few days or even a few weeks.

**Example: Immediate Notification Required**

Seller will contact Buyer immediately should the crop be damaged in any degree by any mechanism (human or natural). Should there be a yield 10 percent smaller or larger than Seller has represented as an expected yield, Buyer will be contacted immediately by seller.

It would be better to replace “immediately” with the phrase “as soon as reasonably practicable.”



- *Farmer May Be Required to Hold Farm Products Until Buyer Able to Receive*

A disaster provision might require a farmer to delay delivery in the case of a disaster suffered by the buyer. This delay may require you to hold or store a crop, livestock, or livestock products until the disaster is over and the buyer can accept delivery. This might be difficult for you if you produce perishable commodities or do not have low-cost storage options available. Consider deleting this kind of requirement if it does not make sense for your operation.

**You may wish to include language allowing you relief from contract obligations if you suffer crop losses due to insect, weed, or disease pressures.**

To do this, just add “crop losses due to insect, weed, or disease pressures” to the list of disasters in an existing disaster clause. These are common issues for both organic and conventional farmers, but are not often included in standard disaster clauses.





## **Is your disaster clause organic-friendly?**

Be aware that even a well-written conventional disaster clause may not go far enough to fully protect organic farmers. That's because, in addition to classic disaster situations, organic farmers should consider:



- 1) the additional occurrences that qualify as disasters for organic farms, and
- 2) the additional consequences that conventional disasters can have for organic farms.

### **Organic Farmers Risk Additional Types of Disasters**

Pesticide contamination and GMO pollen drift are occurrences that could qualify as disasters for organic crops but wouldn't be disastrous for nonorganic or conventional crops. Similar to a natural disaster, pesticide or GMO contamination could make a farmer entirely unable to fulfill organic contract obligations. Also similar to a natural disaster, farmers are unable to fully protect against pesticide or GMO contamination. Thus, it is wise to consider adding these occurrences to the list of disasters in your disaster clause—or include a separate provision excusing you from performing under the contract if an organic-specific disaster occurs.

### **Organic Farms Are More Sensitive to Consequences From Conventional Disasters**

Disasters can also have consequences for organic farms that go beyond the consequences nonorganic farmers might face. For example, in addition to general flood damage to farm property and crop yields, polluted flood waters could contaminate surviving crops, livestock feed, or soil (with garden-variety pollutants, pesticides, petroleum products, or GMOs) beyond levels acceptable under the National Organic Program (NOP) regulations or your contract requirements.

This kind of disaster-related contamination could also result in revocation of your organic certification for at least the crop under contract. If the contamination is too widespread or persistent, you could be forced to take fields out of organic production for up to three years, and some livestock permanently out of organic management.<sup>1</sup>

### Temporary Variances From NOP Regulations

As noted above, a disaster can make it impossible to comply with your contract. Disasters can also make it impossible to fully comply with NOP requirements. Anticipating disaster-related issues, the NOP regulations allow for “temporary variances” as a way to help organic farmers affected by natural disasters, extreme weather, and other organic farming business interruptions.<sup>2</sup> Under these conditions, the regulations allow NOP to create temporary exceptions from organic practices, such as those related to crop rotation, soil fertility, seed, and access to pasture.<sup>3</sup> Note that even in a disaster situation, NOP cannot grant variances to permit the application of prohibited substances; so organic farmers who suffer pesticide or GMO contamination as a result of disaster likely cannot benefit from a variance.<sup>4</sup>



NOP variances are almost always limited to a specific place, crop or livestock type, and time period. For example, due to severe drought in August 2011, NOP granted a temporary variance from the access-to-pasture regulations for organic producers in certain Colorado counties. The variance was limited to those producers with non-irrigated pasture, and expired at the end of the Colorado grazing season.<sup>5</sup>

While you may be able to take advantage of an NOP variance in a disaster situation and maintain continuous organic certification, your contract may not allow the same flexibility. Taking advantage of an NOP variance could cause you to violate contract standards. Consequently, you may wish to consider including language in the contract disaster clause or a separate provision stating that if you take advantage of a temporary NOP variance due to disaster, the buyer will waive any contract provisions that conflict with the terms of the temporary variance.

Livestock producers appear to be the organic farmers most commonly affected by conditions requiring temporary variances, so organic livestock producers should make a special effort to include a contract provision allowing producers to take advantage of NOP temporary variances without violating contract standards.



**Recommendations for Organic-Friendly  
Disaster Clauses:**

- Consider adding language to your contract stating you are released from the contract if your organic crops or livestock are contaminated by a natural or human-caused disaster that is not your fault.
- Consider adding language stating you are released from the contract if your organic certification status is revoked due to a natural or human-caused disaster that is not your fault.
- Consider adding a provision stating that if you take advantage of a temporary NOP variance due to disaster, the buyer will waive any contract provisions that conflict with the terms of the temporary variance.

**Examples: Organic-Friendly Disaster Language**

Force Majeure: If the performance of the party suffering a disaster as described herein is delayed for more than 60 days and/or is substantially impaired, either party may cancel the contract upon written notice. Neither party shall be liable for damages due to delay or failure to perform any obligation under this Agreement if such delay or failure results directly or indirectly from acts of war, civil commotion, riots, strikes, lockouts, interference in telephone communications, carrier delays, fire, flood, windstorms, or other extreme weather events or acts of God, delay or failure to receive raw materials, pesticide contamination, GMO contamination, revocation of organic certification, or any cause of a like or different kind beyond the reasonable control of either party.

NOP Temporary Variance: Buyer and Seller agree that Seller may take advantage of any applicable temporary variances announced by NOP without risk of violating the terms of the contract.

**Consider How You Can Mitigate Disaster Losses**

Think through the various disaster scenarios that could affect your organic operation, and consider whether the disaster clause in your contract is sufficiently clear and detailed—or whether you wish to delete requirements or include additional language.

If disaster does strike your farm, be sure to keep records of yields and sales to show the value of your organic farm products. Take and retain photographs of damaged crops. These records and photographs are important evidence of contract performance that can also serve as evidence of loss for any insurance claims or government disaster assistance you might seek.

In addition to your local Farm Service Agency (FSA) office and the FSA website, a good source of information about federal disaster relief

programs is FLAG's "Farmers' Guide to Disaster Assistance," available for free download at [www.flaginc.org](http://www.flaginc.org).

### **Does the contract require any level of confidentiality?**

Confidentiality provisions appear in organic contracts with some regularity. Depending on the scope of the provision, they can be relatively harmless or a significant burden. Confidentiality provisions can be dangerous because they limit whom you can share contract information with once the contract is signed. It is important that you are able to share the contents of the contract with, at the very least, your spouse, your attorney, your financial advisers, and your lender. For instance, you do not want to end up with a serious contract issue and be faced with the choice between consulting an attorney or being in violation of your contract. You also do not want to risk being denied operating credit because you cannot show your contract to a lender who wants to see it.



**Confidentiality provisions do not apply until after you have signed the contract. Therefore, a confidentiality provision in an unsigned contract does not prevent you from consulting with an attorney or other advisors before signing the contract.**

Rare Exception: If you signed a nondisclosure agreement for the contract negotiation period or otherwise agreed not to disclose information revealed during the contract negotiation period, you are bound by that separate pre-contract confidentiality agreement.

Confidentiality provisions can vary widely, both in scope and in substance. Many confidentiality provisions bind only the farmer and do not bind the buyer at all. It is legitimate to question whether a confidentiality provision that binds only one party to the contract is fair.

Some organic farmers object to confidentiality clauses that restrict farmers' right to share price and contract information with other farmers. When farmers cannot share contract price information, it is very difficult for farmers to shop around for the best price among different buyers. This allows buyers to depress contract prices because they do not have to

compete for suppliers by offering farmers good prices. This situation has already arisen in conventional poultry and livestock markets.

Your state may protect farmers from confidentiality provisions in contracts by making them unenforceable and/or by requiring that farmers be allowed to share contract information with attorneys, lenders, spouses, or other important business advisers. For example, in Minnesota, contracts must not contain provisions that prohibit farmers from “disclosing terms, conditions, and prices” in agricultural contracts, and contract provisions that state otherwise are void and unenforceable.<sup>6</sup> This kind of state law automatically voids some confidentiality clauses, so farmers should check their state’s laws instead of relying only on contract language if there is a question about the enforceability of a confidentiality provision.

If a buyer regularly does business in a state with contract confidentiality laws, the buyer’s standard contract might include a confidentiality provision in one part of the contract but specifically recognize in another part of the contract that farmers in that state are not subject to the confidentiality provision in accordance with that state’s law (see example below).

Example: Recognition of State-Specific Confidentiality Exemption


For Minnesota Producers Only: Producers who are residents of Minnesota or grow crops on land located in Minnesota possess specific legal protections set forth in Chapter 17 of the Minnesota Statutes. Minnesota producers are not prohibited from disclosing terms and prices contained in this agreement, and Minnesota producers have the further right to cancel this contract by mailing a written cancellation notice to the Buyer (at the address listed in Section 1 of this agreement) within three business days after receiving a copy of the signed contract. In case of dispute, Minnesota producers may also make a written request to the Commissioner of the Minnesota Department Agriculture for arbitration or mediation services as set forth in this agreement.



### Common Features of Confidentiality Clauses

Some common features of confidentiality provisions are described below. Please note that a confidentiality provision could combine one or more of the following features to create any number of unique versions.

- *No restrictions* – neither you nor the buyer are required to keep any information confidential.
- *Total restriction* – neither you nor the buyer can share any information about the contract with any person not a party to the contract (third parties). This could even include a requirement to keep confidential the fact that the contract exists.
- *Restriction by individual* – the contract allows you (and/or the buyer) to share information about the contract solely with certain individuals. For example, the provision might require you to keep the contract information confidential as to all third parties except for an attorney, spouse, lender, accountant, employees, business partners, and/or other individuals who need to be informed for business reasons.



Example: Confidentiality Clause Allowing Limited Disclosure to Certain Individuals

Buyer and Producer agree that all information received regarding the Contract, other than publicly available information, shall be held confidential and shall be disclosed only to those individuals necessary to the smooth operations of Producer's organic farm. These individuals include, but are not limited to, legal counsel, immediate family members, financial advisors, lenders, business partners, and organic certifiers.

Some confidentiality provisions might allow you to share contract information with certain advisers or employees, but might also require you to make those individuals sign separate confidentiality agreements. You should consider whether you are willing to ask employees or other individuals sign separate confidentiality

agreements, since this could be burdensome. Additionally, you should consider whether you are willing to enforce those agreements against these individuals on behalf of the buyer, should they be violated.

Example: Confidentiality Clause Requiring Separate Non-Disclosure Agreements

Buyer and Seller agree that all information received regarding the Contract, other than publicly available information, shall be held confidential and shall be disclosed only as required by law, or to individuals necessary to the smooth operations of Seller's organic farm. However, information held confidential shall only be released to said individuals after said individuals have executed separate non-disclosure agreements satisfactory to protect Buyer's confidential and proprietary information.



- *Restriction by type of information* – the contract prohibits you from sharing some information with third parties, but allows you to share other information. For example, the confidentiality provision may prohibit you from sharing pricing information, agricultural production methods, feed composition, trade secrets, or information not in the public domain. You may be allowed to share information already in the public domain (for example, information about the buyer that could be obtained with a Google search or a public records search), or other types of information.





Example: Confidentiality Clause Protecting Buyer's Information

Both parties agree that any of Buyer's trade secret or otherwise proprietary information is deemed confidential, and may not be shared with third parties.

This provision might seem at first glance to bind both parties, but upon closer inspection it becomes clear that only the farmer is bound. The buyer does not agree to protect the farmer's confidential information, making this a one-sided provision in favor of the buyer.

- *Prior written approval required* before sharing any contract information – the contract might require you to obtain written approval from the buyer before sharing any information about the contract. This could be risky, especially if you end up in a contract dispute; the buyer will have an incentive to prevent you from releasing any information to an attorney or other adviser who could help you pursue claims against or defend claims by the buyer.



Example: Confidentiality Clause Requiring Prior Written Approval and Covering More Than Contract Terms

Seller agrees that all information obtained in connection with the instant agreement (including the terms of the agreement itself) shall not be provided to third parties without first obtaining the express, written permission of Buyer.

In this case, not only are the terms of the contract confidential, but any additional information you receive from the Buyer during contract negotiations, contract performance, and any other contract-related activity is also confidential.

- *Extending beyond the term of the contract* – the contract might state that the confidentiality restrictions apply for a certain number of years after the termination or natural end of the contract. If this is the case, consider whether you think the time frame is reasonable.

Example: Confidentiality Clause Extending Beyond Term of Contract

Confidentiality Agreement. The parties agree that the operational information, facility information, transit and delivery processes, customer information, and any other information not in the public domain are proprietary information to be held confidential during the contract term. Moreover, this confidentiality agreement shall survive contract termination, and shall be fully enforceable for a period of three years after termination of this contract.





**If you are offered a contract with a confidentiality clause, you could:**

- Strike it out. A contract without a confidentiality clause is probably best in most cases.
- Negotiate a provision allowing you to share contract information with important advisers (see example on page 4–11 of this chapter).
- Negotiate a provision that only covers trade secrets or other truly confidential or sensitive information (but specifically excludes terms, conditions, and prices of contract).
- Make sure confidentiality is a two-way street. If you must agree to a confidentiality clause, at the very least both the farmer and the buyer should be equally bound to protect each other's confidential information.

**Does the contract require you to guarantee that your farm product is free of security interests or liens?**

Some contracts include language requiring the farmer to guarantee that there are no liens or other creditor claims on the farm products to be sold. The buyer's motivation for including a provision requiring freedom from security interests or liens is likely that:

- (1) the buyer does not want to be held liable if you do not pay your lender from the money received from the buyer as payment for the organic farm products, and/or
- (2) the buyer does not want the responsibility of ensuring that all lienholders are named on any checks paying you for the organic farm products.

If the contract requires that you guarantee your farm product is free of security interests or liens, consider whether you will be able to obtain credit for operating funds or inputs without giving a lender or a supplier a security interest in or lien on your crops, dairy products, or livestock. You should also double-check to be certain whether you have already granted a lender a security interest that would attach to the organic farm products under contract. Some examples of how this could happen include:

- You took out a loan for the current year's production and granted the lender a security interest in that production prior to signing the organic contract,
- You obtained an operating loan for a previous year's production which has not been fully repaid and for which a security interest in your production continues until the loan is paid off (note that some state laws limit the number of years for which a security interest can continue), or
- You obtained a loan in previous years that included a security interest in livestock purchased and its offspring.

If any conditions creating a security interest in the organic commodity under contract exist, you cannot in good faith sign a contract guaranteeing that your organic farm products are free of security interests or liens.

Example: Freedom From Security Interests or Liens Clause

Producer warrants that Producer holds good and marketable title to the contracted crop, and further warrants that said crop is free of any security interest and/or other liens or encumbrances of any kind. If the status of the commodity changes during the term of this agreement, Producer agrees to immediately provide Buyer with written notice and appropriate documentation.



It may be possible to negotiate toward a middle ground with respect to liens and security interests. If you cannot guarantee freedom from liens and security interests, consider promising that you will inform the buyer about any existing (or newly created) liens or security interests so it can include those lienholders or secured parties on its checks to you. If the buyer learns about a lien in the crops, dairy products, or livestock under contract, it will likely wish to make payment jointly to you and the lienholder(s) so as to avoid any involvement in future lawsuits the lienholders might decide to bring if they are not paid in full.



**Example: Better Security Interest/Lien Clause**

Seller agrees to notify Buyer in writing of any security interest and/or other liens or encumbrances of any kind, including those that arise during the course of contract performance.

If you have reason to trust the buyer and are willing to go further, you could agree that you will not give a new lien on the crop or livestock without the buyer's oral or written permission. This could be risky, though, especially if you need to acquire inputs in a short time frame and the buyer is slow about getting back to you with permission (or the buyer refuses to grant permission at all).

**Requirement to Provide Personal Information**

The contract might also require you to give the buyer your Social Security number, federal tax ID number, or other identifying information so that the buyer may conduct a Uniform Commercial Code (U.C.C.) lien search. Most states offer online U.C.C. lien search services allowing a search of any publicly recorded liens filed in that state. However, if giving the buyer this personal information for this purpose makes you uncomfortable, you could suggest language promising you will alert the buyer to all liens instead of agreeing to give the buyer information necessary for an independent search.

**Does your contract require you to carry insurance?**

Occasionally, organic contracts require farmers to maintain insurance policies. This could include federal crop insurance<sup>7</sup> or a private liability insurance policy.

**Example: Insurance Required**

Insurance Policy Required. Grower shall maintain in full force and effect for the duration of this Contract comprehensive general liability insurance coverage with minimum limits of one million dollars (\$1,000,000.00). Grower's insurance carrier shall be acceptable to Buyer, and Buyer shall be named as a co-insured party under the policy. Grower will provide Buyer with proof of insurance, and Buyer shall be immediately notified by Grower of any changes in the policy status.



If your contract does require insurance, you will likely be required to keep the policy current for the duration of the contract (and sometimes longer, depending on the language of the contract). Some buyers will also require you to name them in the insurance policy as an additional insured (meaning that both you and the buyer are protected by the insurance policy). The contract will likely require a specific type of insurance, such as comprehensive general liability or product liability.

Prior to signing the contract, make sure you are actually able to obtain the necessary coverage from an insurance provider. Federal crop insurance is not available for all types of crops in all states, and coverage may not reflect organic market prices. Private insurance availability varies by insurance provider.

Furthermore, insurance can be expensive, and organic crop insurance premiums are often (unjustifiably) higher than conventional crop insurance premiums.<sup>8</sup> If the coverage required by the contract is too expensive, you could try negotiating with the buyer to lower the liability coverage limit (for example, \$500,000 instead of \$2 million) or agree to indemnify the buyer if any claim arises in the course of the contract (see the next section on limitation of liability and indemnification).

If you do agree to an insurance requirement, the contract might also require that you notify the buyer about any changes to the policy terms or coverage. Make sure to follow through on these requirements, or you will risk breaching the contract. To reduce any notice burdens, you could agree to notify the buyer of “major” changes instead of “any” changes.

**Does your contract mention “indemnification” and/or limit the buyer’s liability?**

Indemnification and limitation-of-liability clauses are often intertwined in one long contract provision. It may be helpful to think of your indemnification obligations as having the potential to require you to pay the buyer a lot of money if a problem arises, while limitation-of-liability clauses have the potential to prevent you from recovering money from the buyer.

Many indemnification and limitation-of-liability clauses, as described above, are entirely one-sided in favor of the buyer. This means, for example, that while the farmer may agree to indemnify the buyer, the buyer does not agree to indemnify the farmer. If you must agree to an indemnification clause or a limitation-of-liability clause, it is fair to request that the indemnification and limitation-of-liability clauses bind both parties equally.

**Example: One-Sided, Intertwined Indemnification and Limitation of Liability Provision Favoring Buyer**

To the fullest extent permitted by law, Seller shall save and hold Buyer, its directors, officers, employees, agents, and representatives harmless from and indemnify, defend, and protect such parties against all liability, loss, claims, demands, damage (including damage to property or bodily injury), and expense (including reasonable attorneys fees) arising out of or in any way resulting from Seller's performance or non-performance hereunder, including any defect or nonconformity with Seller's warranties of the goods and services delivered hereunder, any act or omission of Seller, its agents, employees, or subcontractors; any act or omission of any carrier selected and employed to deliver goods ordered hereunder to Buyer; any failure by Seller, its agents, employees, carriers, or subcontractors to comply with the terms hereof; any infringement or claim of infringement of any patent, unpatented invention, copyright, design process, trademark, tradename, brand, slogan, unfair competition, or other adverse rights; or any litigation based on or arising out of the foregoing.



**Indemnification** involves protecting someone else from penalties or liabilities—usually by hiring a lawyer to defend that person and then paying any money that the person owes. Thus, if you sign a contract with an indemnification clause, you generally agree to pay the legal costs and other expenses involved in defending the buyer against a lawsuit by a person not involved in the contract (a third party). Additionally, if a court or settlement agreement requires the buyer to pay money to another person or entity, you would also have to pay that money on the buyer's behalf.

Under most indemnification clauses, the lawsuit against the buyer would have to be at least somewhat related to the contract relationship. For



example, if a truck driver gets in an accident delivering your organic product to the buyer's facility, the truck driver might try to sue the buyer. If you agreed to an indemnification provision, you would probably have to hire a lawyer to defend the buyer against the truck driver.

Indemnification provisions can also come into play in dealing with problems with your product. For example, if you sell sprouts to a buyer and those sprouts happen to be contaminated with E. coli and make the buyer's customers sick, you could be forced to hire a lawyer to defend the buyer against the sick customers' lawsuits, and be forced to pay damages to the sick customers who win their lawsuits. Other types of indemnification requirements could actually require you to sue a third party on the buyer's behalf in order to avoid or minimize damage to the buyer. As you can imagine, these kinds of provisions have the potential to bankrupt your farm with legal fees and payouts, so consider these clauses carefully.

Indemnification provisions might also include notice requirements, meaning you would be required to notify the buyer of any lawsuit or potential lawsuit against the buyer that you learn about.

As mentioned above, many indemnification provisions are one-sided in that they require the farmer to indemnify the buyer, but do not require the buyer to indemnify the farmer. At the very least, any indemnification requirement should be a "two-way street" requiring both the farmer and buyer to indemnify each other.



**Example: Indemnification Provision**

Upon demand, Seller agrees to indemnify, defend, and hold harmless Buyer of and from any and all claims, demands, losses, causes of action, damage, lawsuits, judgments, including attorneys' fees and costs, arising out of or in any way related to the instant Agreement.

As legal fees and costs can quickly reach thousands of dollars, you should pay close attention if you see the word "indemnify" or "indemnification" in a proposed contract. Indemnification provisions have the potential to bankrupt your farm operation and should be deleted, if possible.

### Indemnification Provisions Can Be Limited and/or Capped

Although it is probably best for farmers to delete indemnification provisions before signing an organic contract, the risk of indemnification can be lessened by limiting or capping the provision. Common limitations include restricting indemnity to only those lawsuits caused by your non-performance under the contract, or the misconduct or negligence of you or your employees.

#### Example: Limited Indemnification Provision

Upon demand, each party agrees to indemnify, defend, and hold harmless the other party of and from any and all claims, demands, losses, causes of action, damage, lawsuits, judgments, including attorneys' fees and costs, but only to the extent caused by the misconduct or negligence of a party or a party's employees.

Note that indemnification is a “two-way street” under this provision. Both parties are agreeing to indemnify the other in a limited manner.



You could also try to negotiate a reasonable cap on any indemnity costs (in place of or in addition to limiting the scope). The cap can be any amount that you feel comfortable with.



**Example: Capped and Limited Indemnification Clause**

Upon demand, each party agrees to indemnify, defend, and hold harmless the other party of and from any and all claims, demands, losses, causes of action, damage, lawsuits, judgments, including attorneys' fees and costs, but only to the extent caused the misconduct or negligence of a party or a party's employees. In no event shall the maximum amount paid pursuant to this provision exceed the smaller of \$200,000 or the amount actually paid to Seller under this Agreement, whichever is smaller.

Finally, if you do agree to an indemnification provision, it is wise to try to obtain insurance to help cover any potential costs. You may wish to check with an insurance provider prior to signing a contract to find out: (1) whether you qualify for this kind of coverage, (2) how much coverage (as a dollar amount) you can obtain, and (3) the cost of the coverage.

**Limitation of Liability:** Buyers often attempt to limit their liability, or exposure to lawsuits, by including a limitation-of-liability provision in contracts. These provisions generally list a variety of problems that could occur during the contract relationship and describe how the buyer will be protected from legal liability if any of the problems occur.

You should think about whether any limitation-of-liability provision in your contract seems fair and whether you are unnecessarily limiting your ability to recover from the buyer if something goes wrong. Additionally, the limitation of liability should not extend beyond actions directly related to the contract at issue.

Sometimes, the scope of the proposed limitation of liability far exceeds reasonable boundaries. In general, the buyer should be liable for problems that occur because of misconduct, negligence, or failure to act by the buyer or buyer's employees. It does not make sense for the buyer to be protected from actions the buyer could have prevented.

### Make Limitation of Liability a “Two-Way Street”

Similarly, it is probably fair for you to be liable for your and your employees' misconduct, negligence, or failure to act. However, it may not be fair for the buyer to require you to agree that the buyer's potential liability may be limited while your liability is not limited. If you must agree to allow the buyer to limit liability, consider negotiating the same limitation of liability provision for your farm.

### **Does the contract create rules for your communications with the buyer?**

It is not uncommon for an organic contract to require that the farmer communicate with the buyer regarding the contract in writing. The contract may even describe how the written communication must be transmitted (for example, by certified or registered mail, fax, email, courier, overnight delivery, etc.).

Although it may feel more natural for you to call the buyer to share information or ask questions, if your contract has a provision detailing how communications must be made, you need to follow those directions. If you want any notice or information you give to the buyer to have any effect under the contract, you must communicate according to the contract requirements. If you choose not to, it is possible the buyer could later claim never to have received information you provided. If a dispute arises, information you provide using a means other than what the contract requires may be deemed to have no legal effect under the contract, and may be treated as if the communication never happened. This can happen even if the buyer acknowledges receiving the information.

Thus, for anything important (such as notice of late delivery, disaster, etc.), it is a smart practice to send the appropriate communication to the buyer (even if it is just a letter memorializing a phone conversation). If you are uncomfortable with the level of detail in the contract language describing how communication between you and the buyer must occur, consider negotiating a less complex communication provision. For example, instead of requiring a written communication in a particular manner (such as by certified mail), you might negotiate for a simple writing requirement that allows any type of written communication method (including email, regular mail, fax, etc.).

**Example: Communication Requirements**

Producer agrees to make reasonable efforts to receive communications from Buyer. All communication between the parties related to this agreement shall be in written form, either transmitted by fax or email, sent by reputable overnight delivery courier (FedEx, DHL, or similar), or by certified U.S. mail to the appropriate email address, fax number, or physical address for Buyer contained herein. With the exception of routine operational communications, communication conducted via any other method shall be deemed ineffective.

**Put Everything In Writing!**

Even if the contract does not require communication with the buyer to be in writing, you should still be sure to communicate important contract-related information to the buyer in writing and keep a written record of what you provided to the buyer and when.

It is best to make sure that you keep written records of at least the following:

- (1) Important information provided to the buyer;
- (2) Important information received from the buyer;  
and
- (3) Any agreements reached with the buyer that change or clarify any contract provisions.

It is also a smart practice to write a short letter or email to the buyer restating any important information the buyer communicates to you in a meeting or over the phone that asks the buyer to respond within a certain time period (for example, 10 days) if it does not agree with your restatement of the information.

**CHAPTER 4 – ENDNOTES**

- <sup>1</sup> See 7 C.F.R. §§ 205.202(b), 205.671 (2012); but see 7 C.F.R. § 205.672 (2012). See also Jim Riddle, *Flooding and Organic Certification Webinar* (eOrganic eXtension 2011), available at <http://www.extension.org/pages/60874/flooding-and-organic-certification-webinar>.
- <sup>2</sup> See 7 C.F.R. § 205.290 (2012).
- <sup>3</sup> See 7 C.F.R. § 205.290(a) (2012).
- <sup>4</sup> See 7 C.F.R. § 205.290(e) (2012).
- <sup>5</sup> See U.S. Department of Agriculture, Agricultural Marketing Service, *Current Temporary Variances List* (2012), available at <http://www.ams.usda.gov/AMSV1.0/getfile?dDocName=STELPRDC5091045>.
- <sup>6</sup> Minn. Stat. § 17.710 (2011).
- <sup>7</sup> See Midwest Organic & Sustainable Education Service (MOSES), *Crop Insurance for the Organic Farmer* web page, available at <http://www.mosesorganic.org/cropinsurance.html> (provides information and links to resources related to federal crop insurance, including the limits of federal crop insurance for organic farmers).
- <sup>8</sup> See National Sustainable Agriculture Coalition, *Organic Crop Insurance Senate 2012 Farm Bill Floor Debate, Making the farm safety net work for organic farmers* (June 2012), available at <http://sustainableagriculture.net/wp-content/uploads/2012/06/Organic-Crop-Insurance-Amendment-Senate-Floor-6-14-12.pdf>.

# 5

## Duration, Termination & Cure

- [5-1](#) When does the contract begin and end?
- [5-1](#) Can the contract be renewed?
- [5-2](#) Will the contract last long enough to allow you to recover any investments?
- [5-3](#) Could the contract end early?
- [5-3](#) Types of termination clauses
- [5-8](#) Does the farmer have termination power?
- [5-11](#) Do you have any rights or responsibilities after termination?
- [5-14](#) Can you fix a broken contract promise?

### CHAPTER QUICK TIPS

#### **Beware of Termination Clauses**

Watch out for provisions that allow termination for any reason or for minor contract violations. These provisions can be replaced with language allowing termination only in cases of serious breach by the farmer or buyer. This kind of breach is often called “material breach.”

#### **“Discretion” Is Code for “Whatever I Want”**

The term “discretion” is often used in contracts. “Discretion” usually means that one party has the power to make whatever choice it wants to make about a particular topic. Farmers should be careful if a contract gives the buyer “discretion” in any respect.





## **DURATION: HOW LONG WILL THE CONTRACT LAST?**

### **When does the contract begin and end?**

Be sure to understand when the contract begins, or “becomes effective.” All of your contract obligations begin on the day the contract begins, so it is important to know when you have to start making sure you are complying with the contract terms.

Make sure you understand exactly how long the contract is intended to last. Some contracts state clear start and end dates. Others are seasonal, and still others are renewable every year or every few years. Some contracts are more vague, using production cycles to determine length of the contract. For example, the duration of egg and poultry contracts is typically measured in numbers of flocks. If you have a flock-to-flock contract, especially for broilers, these contracts can be terminated after a very short period of time.<sup>1</sup>

### **Can the contract be renewed?**

Does the contract have a renewal provision? If so, how is the contract renewed? Is it automatic, or does it require some sort of action by one or both parties? If you understand how renewal of the contract could happen, you will be less likely to become locked in an unfavorable contract by unintentionally triggering renewal, or miss an opportunity to maintain a positive contract relationship by unintentionally failing to renew.

If the contract does not have a renewal provision, consider whether you might like to add one that could make it easier to maintain an important contract relationship. Be sure to clearly state the conditions for renewal and how renewal could be accomplished.

**Will the contract last long enough to allow you to recover any investments?**

Before signing, consider carefully whether the contract period is long enough for you to recover any investments you must make to carry out your contract obligations. If the commodity you will be producing and selling under the contract requires you to make investments—purchasing specialized equipment, constructing new facilities, etc.—you should carefully consider the contract duration and whether the buyer will have the power to terminate the contract early (see next section). If the contract could end before you have the chance to recover your investment from earnings under the contract, how will you replace that income? Can you rely on there being another market or buyer for your production after the contract ends? If not, you may wish to reconsider the risk you are taking by entering into a contract that requires investment but can end before you recover your costs.

## **TERMINATION: COULD THE CONTRACT END EARLY?**

Most contracts include at least a few ways a contract could terminate before its natural endpoint. Termination provisions are often complicated and might be scattered throughout the contract documents. It is important to fully understand how and when your contract could be prematurely terminated so you do not unintentionally lose a contract you are depending upon.

It is smart to go through the contract and identify all of the ways the contract could end earlier than expected.

### **Types of termination clauses**

#### **Termination at Will**

Sometimes, a contract states that it can be terminated at any time and for any reason. Usually, but not always, the party who wishes to terminate the contract for any reason is required to provide advance written notice of termination to the other party.

- *Termination for Any Reason, Without Notice*

You should think carefully before entering into a contract that can be terminated for any reason, at any time, without notice. This type of contract can evaporate without warning. Thus, if your goal is to obtain financial security for the upcoming months, this kind of contract will not help you. However, if you are not worried about the deal falling through (perhaps because you have other marketing options or because you believe the buyer truly needs your production), a contract like this can at least lay out the ground rules if the contract ends up being fully performed.

Regardless, you should be aware that signing a contract that can be terminated at any time without notice could leave you without a buyer in a heartbeat. It would be better to at least negotiate a notice period, as discussed below.

- *Termination for Any Reason, With Written Notice*

Although it is risky to sign any contract that can be terminated for any reason, requiring a written notice period at least gives you some time to look for a new buyer.

Example: Termination for Any Reason With Written Notice

The Buyer may terminate this Agreement, with or without cause, at any time, upon 90 days' prior written notice to the other.

Note that this language gives only the buyer the power of termination—the farmer has no termination power. This language would be more favorable if you replace “The Buyer...” with the phrase “Either party...”



If the contract allows for termination for any reason after a written notice period, make sure the notice period is long enough for you to find another buyer or take whatever other steps you need to continue your operations without too much disturbance. For example, 30 days' notice might be too short, while 90 days' notice might be adequate.

Blanket Breach: Termination for Any Contract Violation

Instead of allowing parties to terminate a contract at will, contracts often limit termination to situations where one party has violated—or “breached”—a contract provision. The broadest of these provisions allow termination for any breach (major or minor) of any contract provision. These so-called “blanket breach” provisions are risky because even a trivial contract violation that does not affect the main purpose of a contract (buying and selling organic crops or livestock) could lead to termination.

In a blanket breach situation, non-breaching parties are not required to terminate due to a breach, but they have the power to do so. For example, if the contract specifies that notification must be sent by certified mail but one party uses registered mail, the other (non-breaching) party could use this minor breach to get out of the contract if the contract also contains a blanket breach termination clause.

Be aware that signing a contract with this type of provision can make any less-than-perfect contract performance a potential problem.



Example: Blanket Breach Termination

Default, Breach: Each party may terminate this Agreement if the other party breaches any part of this Contract.

Farmers who encounter this type of provision should seriously consider trying to negotiate deletion of the provision or change to require “material breach” (discussed on page 5–7 of this chapter) as a termination trigger.

- *The Risk of Blanket Breach Termination Provisions in Combination With Vague Contract Provisions*

As discussed in Chapter 3 of this guide, contract language that is vague or unclear can create significant problems when differences arise. This is particularly true if the contract states that it can be terminated if any part of the contract is breached. You may believe that you are fulfilling all of the contract requirements, but if the buyer understands the requirements differently because the language is unclear, the buyer could claim that there is a breach and seek to terminate the contract. The danger from the combination of vague requirements and blanket breach termination can be difficult to spot when first reviewing a contract because often the termination clause is in one section of the contract and the vague provision is in another section.

Example: Blanket Breach + Vague Provision

One part of the contract states:

D (4). Producer agrees that farm premises shall be kept in an aesthetically pleasing condition.

And, in another section, the contract also states:

J (1). Buyer may terminate this agreement if Producer breaches any term described herein.



A contract with the provisions in the example above could easily allow a buyer to terminate by claiming that your farm is not “aesthetically pleasing” on a particular day. This claim is hard to defend against because “aesthetically pleasing” is a vague term that means different things to different people.

A more subtle way that this combination of provisions could cause difficulty is if a buyer attempts to use a minor breach as leverage. For example, a buyer could say, “Well, you committed a minor contract breach, and I could cancel the contract...but I won’t if you agree to accept a lower price.” In that situation, unless the buyer is bluffing, you are faced with the unpleasant choice between no contract and a lower price.

**If You Encounter a Blanket Breach Termination Provision:**

- Replace it with a provision that allows termination only for material breach—not for minor breaches. See below for a discussion of material breach.

If you cannot replace the term with a material breach term:

- Try to get the blanket breach term deleted.

**If You Encounter a Blanket Breach Termination Provision + Vague Provisions:**

- In addition to the recommendations above on blanket breach, try to make the vague provisions more specific. For example, instead of agreeing that your farm will be kept in an “aesthetically pleasing condition,” you could agree that, “Trash will be removed from farm buildings daily.”

Or, if you cannot clarify vague provisions:

- Try to delete the vague provisions.

**Termination for Material Breach**

Because contract termination can cause serious financial loss, some farmers may never feel comfortable signing a contract that can be cancelled for any reason, even with a long notice period. Similarly, the risk of termination for even a trivial violation may make a blanket breach termination provision unappealing. As an alternative, consider negotiating a provision that allows the contract to be terminated only if certain, significant contract requirements are not met (“material breach”).

So-called “material breach” is a contract violation that has a significant effect on contract performance and damages or destroys the value of the contract for the other party. Material breach generally involves the timing, quantity, and quality of delivering what was promised and is not concerned with how the parties carry out their obligations. However, parties can also specifically identify as “material” any requirements that might not seem significant but that

they particularly want to be carried out to the letter. For example, a buyer might specify that the farmer's failure to use a particular mix of feed would be material breach, or that a farmer's failure to provide notice of potential crop loss within a certain period would be a material breach.

Example: Termination Only Upon Serious (Material) Breach

Either party may terminate the contract only upon the other party's material breach of the agreement.



Some contracts provide for termination based either on any (blanket) breach or only for material breach depending on the timing or other measurable factors. For a non-agricultural contract, the type of termination available might depend on how long the contract has been in effect or how much of the contract has been fulfilled. For agricultural contracts, the line between termination for any breach and termination only for material breach is typically determined by the production cycle for the commodity under contract.

Example: Termination for Any Breach or Material Breach Depending on Time in Production Cycle

Either party may terminate the contract upon 60 days' written notice for any reason prior to the Grower commencing planting. After Grower commences planting, the contract may be terminated only upon the other party's material breach.



### **Does the farmer have termination power?**

Termination provisions might allow either party to terminate the contract under certain conditions. However, some contracts are one-sided and allow only the buyer to terminate the relationship.





Example: Buyer-Only Termination Provision

The Buyer may, in its sole discretion, terminate the instant Agreement at any time.



**“Discretion” Is Code for “Whatever I Want”**

The term “discretion” is often used in contracts. In a contract, “discretion” usually means that one party has the power to make whatever choice it wants to make about a particular topic. In the example above, “in its sole discretion,” means the buyer can terminate the contract at any time, for any reason.

Farmers should be careful if a contract offer gives the buyer “discretion” in any respect.

Review the contract termination provisions carefully to determine whether the contract allows you to protect yourself if problems arise or the buyer fails to keep important contract promises. If not, consider negotiating language to protect yourself.

Termination for Buyer’s Failure to Keep Contract Promises

Suppose you are contractually obligated to plant a certain type of identity-preserved seed, and the buyer fails to deliver the seed on time. As a result, you face missing an important planting window and ending up without a crop (or with a low-quality or low-yield crop). In that situation, it would be helpful if the contract gave you an avenue to exit the contract relationship in time to plant substitute seed.

As discussed in Chapter 3, however, termination is not the only possible response to a buyer’s failure to keep contract promises. Because you may ultimately want to continue with the contract even after the buyer’s breach, consider including language that allows you to choose a less severe penalty, such as money damages or a relaxing of your own obligations.

### Termination Upon Buyer's Purchase or Merger

If the identity of the buyer you are dealing with matters to you, consider negotiating a provision that would allow you to terminate the agreement if the buyer is bought by or merged into another company. Consider whether it is important for you to have termination power in this kind of situation.

### Termination Upon Buyer Becoming Insolvent or Filing for Bankruptcy

Organic contracts frequently state that they may be terminated if one party becomes insolvent, enters bankruptcy proceedings, or otherwise goes out of business.

#### Example: Termination Upon Insolvency or Bankruptcy

Upon written notice, either party may terminate this Agreement if the other party becomes insolvent, makes a general assignment for the benefit of creditors, becomes subject to any bankruptcy proceedings, has liquidated, or has ceased operations.



However, if a party to a contract files for relief in bankruptcy, bankruptcy law may override the type of termination clause shown in the box above. In most cases, bankruptcy law will allow the buyer in bankruptcy (known as the “debtor in possession”) or the bankruptcy trustee to assume or reject the contract as they wish.<sup>2</sup> If the buyer in bankruptcy or the trustee assumes the contract, the contract would continue despite the bankruptcy termination clause. If they reject the contract, the contract would be terminated even if the farmer wanted to continue the contract relationship. Because bankruptcy is a complicated and technical area of law, if the buyer files bankruptcy, it would be a good idea for you to consult a bankruptcy attorney.<sup>3</sup>

See Chapter 12 for more detailed information about both farmer and buyer bankruptcy issues, including some ways to get paid while the buyer is in bankruptcy. The bottom line is that bankruptcy is very complicated, making it all the more important for farmers to investigate the financial stability of the buyer before signing a contract.

### Termination Upon Farmer's Serious Illness or Death

If you become seriously ill or disabled, can you terminate the contract, with or without penalty? If you pass away during the contract term, will the contract end? If one of these terrible things comes to pass, would your farm business or your family be forced to shoulder the remaining contract obligations, or might they want to continue under the contract but be denied the opportunity? Consider whether you should try to negotiate a provision protecting you and your family if you are no longer able or alive.



#### Example: Termination Upon Serious Illness or Death

Upon Grower's serious illness, disability, or death, Grower (or Grower's estate) shall have the power to terminate the contract upon written notice.

This provision allows your family or the person representing your estate to terminate the contract if they so choose, but does not require termination.

### **Do you have any rights or responsibilities after termination?**

#### Rights:

If the contract is terminated early, will you be reimbursed for your efforts up to the date of termination? The answer is: "Maybe, but probably only if you have provided the buyer with something of value as part of the contract relationship."

Most organic contracts do not expressly provide for reimbursement for farmer efforts upon early termination. Contracts that do provide for reimbursement upon termination almost always involve the farmer providing some sort of valuable service or product to the buyer before the end of the contract period. For example, if you provided consulting services or delivered organic crops or livestock before the contract's early termination, the contract might require the buyer to pay you for the value of those services or products even if the contract terminates early.

However, even if the contract does not expressly require payment for services or goods provided to the buyer in an early termination situation, courts generally require parties who have benefited under a contract to

compensate the other party for those benefits, even if the contract is terminated or made unenforceable. This is called “preventing unjust enrichment.” Still, it is important to note that, if the buyer will not voluntarily pay you for those services or products, you will likely have to go to court in order to get paid.

Note that courts will generally not require a buyer to pay for work done by a farmer prior to early termination that does not benefit the buyer. For example, even if you expend thousands of dollars and hundreds of hours planting, tending, and harvesting an organic red wheat crop, if the contract terminates before you deliver the crop, the buyer will likely owe you nothing under an unjust enrichment theory because you have not yet provided the buyer anything of value (the wheat).

#### Responsibilities:

If you could be left with expensive or time-consuming responsibilities should the contract be terminated, consider whether your operation could survive that kind of disruption or financial burden. For instance, would you be required to reimburse the buyer for seed or other inputs if the contract is terminated early?

Alternatively, are you required to send seed, plants, breeding stock, or other inputs to back to the buyer if the contract is terminated? Some buyers include this type of provision to protect their interest in identity-preserved seed or breeding stock. Unfortunately, this type of requirement could cause serious disruption to your operation if you are not allowed to bring your crops to harvest or your livestock to full growth. In this situation, consider negotiating different language—perhaps a provision that allows you to choose between reimbursing the buyer for the cost of inputs and sending back seed, plants, or other inputs.

Organic contracts may also specifically state that certain provisions are intended to continue in effect after termination. For instance, a confidentiality clause that states it extends three years past the end of the contract would still be in force even after an early termination. Sometimes a contract includes a list of the provisions in the contract that are intended to continue in effect even after termination.



Example: Provisions Surviving Termination

Survival of Termination. The following sections shall survive termination of this Agreement: A, F, G(ii), J, and L(i)(a).

When deciding whether to enter into an organic contract, be sure to consider whether any responsibilities that survive the contract will interfere with your future operation.

## CURE: CAN YOU FIX A BROKEN CONTRACT PROMISE?

Sometimes, a contract will set out how a broken contract promise can be fixed. Fixing a broken contract promise is called “cure,” or “curing a breach.” A cure provision creates a middle ground for the non-breaching party between accepting the breach and having to terminate an otherwise desirable contract. Many organic contracts provide that a contract will terminate if a breach “remains uncured” for a certain number of days. Often, a cure provision will be stated together with termination language.

### Example: Intertwined Blanket Breach Termination and Cure Provision

Default, Breach: Each party may terminate this Agreement if the other party breaches any part of this Contract. If the breach is capable of cure, the breaching party must cure the breach within 14 days. If the breaching party fails to cure, termination is effective after the 14-day cure period expires.



It can be helpful to include contract language that describes some specific ways each party can cure specific broken contract promises. If you know exactly how to cure a breach, you can avoid disagreements about whether you have successfully cured a breach, and can be more certain to avoid breach or contract termination. Alternatively, the contract could require the buyer to notify you of a breach and describe the cure (if cure is possible). This kind of requirement would prevent a buyer from purposely failing to notify you of a breach until after the cure period had expired, effectively terminating the contract.



**Example: Notice of Breach and Specific Cure Provision**

In the event of breach, the non-breaching party must notify the breaching party of the breach within 48 hours. If the breach is capable of cure, the non-breaching party must also describe to the breaching party how the breach can be cured and a reasonable deadline by which any cure must be completed.

On the organic farmer's side, an example of cure could be removing a crop lien within a specified period or accepting a discounted price for low-quality deliveries (in lieu of total rejection). Curing a breach could also involve delivering a substitute product, delivering within a certain time frame, allowing access to records, or otherwise bringing your activities up to contract standards. For a buyer, cure could involve paying a penalty or premium price.

**CHAPTER 5 – ENDNOTES**

- <sup>1</sup> Broiler chicken production contracts traditionally have guaranteed only one flock of birds delivered to the farm. Under a flock-to-flock contract, if a buyer decides to continue with a grower for a new flock, the same contract terms would remain in place for each subsequent flock delivered to the farm; but the buyer is free at any time to choose not to continue with the grower for any additional flocks. Some broiler contracts even state a time period for the contract, such as “three years” or “five years,” but do not guarantee delivery of more than one flock during that period. These contracts also often allow the company to end the contract at any time for any reason it chooses—even if the stated contract period has not ended.
- <sup>2</sup> See 11 U.S.C. § 363(l), 365 (2012).
- <sup>3</sup> See 11 U.S.C. § 365(e)(1) (2012). This statute generally makes “termination upon bankruptcy” provisions unenforceable in so-called “executory contracts.” An executory contract is a contract where one or both parties have not fulfilled their obligations at the time of the bankruptcy filing. See also 11 U.S.C. § 541(c) (2012). A clause that terminates a contract because of the “insolvency” or “financial condition” of the debtor, or due to the filing of a bankruptcy case, will be unenforceable once a bankruptcy case has been filed. See, for example, Bob Eisenbach, *Are “Termination on Bankruptcy” Contract Clauses Enforceable?* (The Business Bankruptcy Blog, September 16, 2007), available at <http://bankruptcy.cooley.com/2007/09/articles/business-bankruptcy-issues/are-termination-on-bankruptcy-contract-clauses-enforceable/>.



# 6

# Price, Quantity & Quality

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## CHAPTER QUICK TIPS

### **Always Take Samples For Yourself**

Even if the contract does not require you to submit samples, it is always smart to take and keep samples of your organic products for yourself. Maintaining reliable samples can help you prevent or settle a quality dispute.

### **Buyers Should Pay for Produce Within 30 Days**

To avoid losing important rights to payment under federal law, farmers who sell produce should require buyers to pay within 30 days from the date the buyer accepts produce.



# PRICE

## How is the base price determined?

Base pricing methods in organic contracts vary widely. Further complicating matters, the base price is usually just the starting point for calculating the price the farmer will actually receive. Farmers must generally factor in discounts, premiums, and potential deductions for cleaning, transport, and other services. Still, the base price will have a big impact on the farmer's overall profit, so it is wise to carefully scrutinize base pricing methods.

For any pricing method, it is helpful to ask the following questions:

- Are the provisions describing pricing and the method of calculating payment clear? If not, consider negotiating clearer language.
- Are any of the payment criteria (such as quantity and quality) out of your control? If so, consider negotiating limitations on the buyer's power to control payment criteria.
- Is the price calculation fixed, or is it dependent on future conditions?
- How do the best- and worst-case scenarios under the contract's pricing method affect the final price at delivery?
- Is the method of calculating payment appropriate for your operation?

## Common Base Price Methods

- *Is the price a flat rate negotiated at the time the contract is signed?*

A flat rate set at the time the contract is signed reduces uncertainty and creates a more certain financial outlook for the farmer by protecting against falling market prices. However, the farmer has

also given up the chance to profit from any increase in market price at the time of sale.

- *Is the price tied to the cost of inputs?*

A base price tied to the cost of inputs can protect the farmer from spikes in input costs, and can therefore be highly beneficial. For example, is the contract price for organic dairy products linked to the market price for organic grain? Does the price the farmer receives increase or decrease as organic feed prices rise or fall?

Prices tied to inputs might be calculated as a set base price plus (or minus) a certain amount based on the cost of inputs. If the base price is linked to the market price of grain or some other input, make sure you understand the linked price calculation and whether it is advantageous for the product you are selling.

- *Is the price determined by the organic market or linked to the organic market price for the product (for example, a certain percentage of the organic market price or the organic market price plus a certain amount)?*

A base price term determined by the market price for the product is not as helpful in reducing uncertainty and protecting farmers from falling market prices. However, it can allow farmers to take advantage of increases in market prices over the course of the contract. Still, organic farmers who agree to contracts with a base price linked to the market for their product should be aware that this kind of price provision requires more detail to avoid uncertainty.

If the contract's price provision is linked to your product's organic market, it is a good idea to include in the contract language about the following:



- Who determines the organic market price for contract purposes (the farmer or the buyer), and how?
- Is the market price tied to an institutional report (such as the USDA Agricultural Marketing Service reports for organic grain, feed, seed, poultry, eggs, and dairy) or tied to another standard?
- When is the market price determined? Timing can significantly affect the price paid.
- What is the geographical boundary of the market? For example, in determining the market price for organic grain,

is the market price the national price, the Eastern Cornbelt price, or the Upper Midwest price?



Example: Vague Market-Linked Price Term

Price Term: Current organic market price feed grade oats plus \$0.55 per bushel.



Example: More Detailed Market-Linked Price Term

Price to be determined based on organic market price for feed grade oats as reported in the bi-weekly USDA Eastern Cornbelt Organic Grain & Feedstuffs Report for the final week of September, 2012.

- *Can the buyer change the base price during the contract?*

If the buyer can change the base price during the contract, the buyer has the power to change the farmer's entire cost-benefit calculation of the contract. Although this is an increasingly common feature of organic dairy contracts with the large dairy buyers, signing a contract that allows the buyer to change the base price during the contract is a risky proposition for any farmer.

**Example: Buyer Can Change Base Price During Contract Term**

Buyer shall pay Producer for organic milk at the Base Price referenced herein per cwt. Buyer may, at its sole option, increase or decrease the Base Price upon 30 days' written notice to Producer. Notwithstanding the foregoing, a decrease in the Base Price of greater than 20 percent shall require Producer's written approval.



If you cannot avoid this kind of provision in your contracts, try to negotiate:

- a reasonable notice period (perhaps longer than 30 days);
- a price floor below which the base price cannot go;
- a requirement that any further downward adjustment to the new base price must have the farmer's written agreement;
- language stating the farmer can cancel the contract without penalty if the farmer does not agree to the lower base price.

**Does the contract include a clearly defined process for earning premiums and taking discounts?**

The final price a farmer receives for organic farm products will almost certainly be linked to the quality and quantity of the products delivered. It is quite common for organic contracts to include premiums for products that exceed set quality levels and discounts for products that fall below quality standards.

Some questions to consider related to premiums and discounts include:

- What are the premium/discount criteria, and who determines when the criteria are met?
- How are premiums and discounts calculated?

- Can you examine the calculations used to determine the amount of premium or discount in order to verify whether the calculation was done correctly?

Be cautious of contract language that allows discounts determined entirely at the buyer's discretion. All premium and discount calculations and criteria should be clearly spelled out in the contract, so each party knows exactly what to expect.



Example: Discounts to Price Term

Discounts will be taken at Buyer's sole option and will depend on the amount of deviation from quality standards at the time of delivery.

If the contract language leaves it to the discretion of the buyer when to take a discount and/or the amount of the discount taken, you may want to consider negotiating a specific discount scale. If you do not want to set a discount scale in advance, you and the buyer could agree to negotiate a discount rate at the time of delivery. However, because farmers are typically in a weaker bargaining position and are less likely to just walk away from a deal when the product is sitting at the buyer's door, waiting could cause you to later agree to a higher discount rate than you might have agreed to at the time you signed the contract.



Example: Price Discounts Negotiated at Time of Delivery

If all or part of the commodity is nonconforming, Buyer may reject all or part of the commodity, or the price may be discounted by mutual agreement of the Buyer and Seller.

## **Can the buyer take price deductions unrelated to quantity or quality?**

Watch out for contract provisions that allow the buyer to take deductions for costs unrelated to the quantity of product delivered, the quality of your product, or even whether you keep your other contract promises.

### **Consider Deleting Language Allowing Deductions for Factors Out of Your Control**

Some organic contracts might include deductions for costs incurred by the buyer “related to the Seller’s contract duties or responsibilities.”

This kind of broad language leaves farmers extremely vulnerable to deductions for a wide range of potential costs that could be deemed “related” to contract obligations, including the buyer’s labor costs for unloading deliveries or the cost of overnighting paperwork.

Seriously consider negotiating the deletion of any contract language that allows the buyer wide latitude to make deductions from the contract price.



## **When will you get paid?**

It is helpful for the contract to include language stating exactly when payment will be made. This reduces uncertainty and ensures the payment schedule satisfies the farmer’s cash flow needs. It can be beneficial to negotiate a payment deadline that is close to the delivery date. Organic contracts vary widely on payment timelines—payment might be prior to delivery, upon delivery, or a certain number of days after delivery.

Contracts may also create conditions that have to be met in addition to delivery before payment will be made. For instance, before getting paid the farmer may be required to request payment, provide an invoice, provide certain certifications, or wait until after inspection, cleaning, or other quality verification (including potential laboratory testing).





**Protections Against Late Payment for Farmers Who Sell Organic Produce:**

If you sell fruit, vegetables, or other produce, and the buyer accepts the produce but fails to pay you (1) fully and (2) promptly, you may be able to recover the unpaid amounts (plus any losses caused by the buyer's failure to pay fully and promptly) by filing a complaint under the federal Perishable Agricultural Commodities Act (PACA). You can file a PACA complaint even if the buyer paid you part of the contract price.

Under PACA, buyers are required to pay the full contract price within the time frames PACA establishes (typically 5-20 days), unless the contract states a different payment deadline.

**\*\*\*IMPORTANT NOTE:**

Farmers who sell produce should avoid entering into agreements extending the time for payment beyond 30 days from the date the buyer accepts the produce.

If a farmer agrees to extend the time for payment beyond 30 days from the date of the buyer's acceptance, the farmer will lose the right to claim payment through PACA's statutory trust should the buyer file bankruptcy or go out of business.

Before agreeing to any payment extension, farmers should consult with an attorney familiar with PACA to determine whether using particular contract language could cause you to lose any rights under PACA. Please see Chapter 12 for more information about PACA rights and complaints.

Try to assess what might be reasonable conditions of payment and what might be too burdensome. Also try to determine how long processes like inspection, cleaning, or testing could delay payment. The bottom line is that you should be able to make an informed decision based on contract language about how long it could take for you to get paid and whether your cash flow needs can be met given the timing of payment.

**Buyer Penalties for Late Payment**

Does the contract provide for any penalties against the buyer for late payment? You may wish to include language that requires the buyer to

pay a cash penalty or take some other action if payments are late. This kind of provision can give a buyer who might otherwise be careless about paying you an incentive to be more prompt with payment.

Example: Penalty for Late Payment

Payment shall be received by Seller within 10 business days of delivery. Buyer shall be assessed a penalty of 1 percent of the contract price for each day payment is delayed.



Laws Providing Protection Against Buyer Non-Payment

Federal Protections: Two major federal laws, the Perishable Agricultural Commodities Act (PACA) and the Packers and Stockyards Act (PSA), provide trust protections for farmers to ensure that there will be money available to pay farmers for agricultural commodities even if the buyer is insolvent, in bankruptcy, or has already used the money for something else. See Chapter 12, pages 12–10 through 12–12, for more information about trusts and other federal protections for some farmers who do not receive full and prompt payment.

State Protections: Some states have agricultural production lien laws to protect farmers' payment rights. Under some circumstances, these laws can provide farmers with a lien on farm products delivered to buyers. These liens are designed to help farmers secure payment from buyers.



**Do Not Let Your Contract Interfere With State Lien Protections**

If you live in a state with farm lien protections, it is a good idea to ensure that your contract does not interfere with your state agricultural production lien rights. For example, you should be very wary of contract language stating that the buyer purchases your organic farm products free of all security interests or liens. You may wish to pay special attention to this kind of language if you are concerned about the buyer's solvency or have had trouble getting paid in the past.

One state lien protection law is the Minnesota Agricultural Producer's Lien Statute, Minn. Stat. § 514.945, which applies to all agricultural commodities except grain and raw milk. California also provides producer lien protection under Cal. Civ. Code §§ 55631-55633 for all agricultural commodities sold to a processor. Check with an attorney licensed in your state to see whether your state has any agricultural lien protection laws.

## QUANTITY

The quantity of organic product under contract can be determined in a variety of ways. It is important to understand exactly how the quantity will be determined for a particular contract and the potential consequences of that type of quantity determination.

### **Is the quantity set at a specific amount of product?**

Does the contract require that you deliver a specific quantity of organic product? For example, is the quantity set at 1,000 bushels of corn, 20 pallets of eggs, or 575 cwt of raw milk per month? This type of quantity term has the benefit of allowing the farmer to know exactly how much product the buyer will purchase at the time of delivery. However, if the contract requires delivery of a specific quantity and your expected output falls short, you could be forced to purchase product on the spot market (or dip into any reserves you might have) to make up the difference. On the other hand, if you have a bumper crop and your buyer is not interested in purchasing your excess output, you may have to look for a buyer on the spot market for the extra production.

### **Is the quantity based on production level?**

Rather than being a specific volume or weight of product, the contracted quantity might be identified as the entire amount of product from a certain number of acres or a certain number of livestock. For example, you could promise to provide the buyer with the entire crop harvested from a specific number of acres. Thus, even if you have a poor crop or a bumper crop, you do not have to worry about either making up for a shortfall or finding a buyer for the excess harvest because you have merely promised to deliver whatever those acres produce.



Example: Quantity Based on Production Level

Buyer will purchase 100 percent of the crop produced from the 50 acres on Seller's property listed as the "Northwest Plot" on the plat attached and incorporated as part of this agreement.

Detailed Descriptions Are Best

If you decide to sign a contract with the quantity based on your production level, make sure the contract includes a detailed description of the crop acreage or the livestock covered (and the fact that the contract is for an organic product). A precise description for crops would include the type of crop, the number of acres, and the legal description or identification of the land on which the crop is grown. For livestock, a description might include the type and number of animals, the location where they are being raised, the identification of a specific flock or herd, or (if the specific animals are tagged, branded, or otherwise individually identified) a list of the tags or identifying marks. You do not want to end up in a dispute with a buyer over which fields your wheat was supposed to be harvested from or which animals were supposed to be sold for slaughter—especially if some fields' production or some animals result in losses or are of poor quality.

Be Cautious About Written Production Estimates

It might seem reasonable to estimate the expected production from the acreage or livestock covered by the contract, and to record the estimate in the contract. However, this can be risky. If your output far exceeds expectations, or if the market price drops far below the contract price, the buyer might refuse to take delivery of anything more than the estimated amount stated in the contract. To protect yourself, you could include language clearly stating that the buyer agrees to purchase your entire production, even if it is significantly different from any estimate. As a further protection, you could give your estimate as a range. For example, instead of stating that you estimate 30 bushels to the acre, you could state that you estimate 25 to 35 bushels to the acre. Alternatively, you could consider keeping your estimates out of the contract itself.

### Can the Quantity Be Changed During the Contract?

Watch out for contract language giving the buyer the right to change the quantity during the contract. This kind of provision can be very risky if you cannot find another buyer for any surplus resulting from the change or do not have enough of your own production to cover an increase and have to make purchases on the spot market to meet your new contract obligations.

Provisions allowing changes in quantity are rarely seen outside contracts requiring frequent deliveries throughout the life of the contract, such as those for eggs, dairy, and livestock. At the very least, quantity change provisions should be accompanied by a significant notice period that may allow the farmer to adapt to the new required quantity.

#### Example: Seller Able to Decrease or Increase Quantity

Buyer retains the right to decrease or increase the agreed quantity. Buyer will purchase by up to 10 percent upon 60 days' written notice.



If you are presented with a contract provision allowing the buyer to decrease the contracted quantity, you should consider whether the contract would still be worth signing if a quantity change occurred—and whether you could find another market for your excess production.

Similarly, if the contract allows the buyer to increase the quantity, you should consider whether the contract would require you to deliver that additional amount even if your production level or yield is not high enough to cover it. Put another way, think about whether the contract could require you to purchase additional product to fulfill an increased contract quantity.

### Can the buyer manipulate the quantity after delivery?

Often, buyers will pay farmers based on the amount and quality of the organic commodity delivered. In some situations, such as when a buyer has received more of a particular commodity than it has demand for, the buyer may not want to pay for the full quantity delivered even though

it was called for by the farmer's contract. In this situation, some buyers may attempt to manipulate the quantity measurement.

To limit this kind of activity, the farmer could try to negotiate contract language allowing the farmer to be present when the delivered commodity is weighed (either in person or electronically through videoconference technology) or requiring the weight to be certified by a neutral third party. The parties could also agree that the commodity will be weighed before delivery to the buyer and that an official weight certificate (such as an Official Grain Weight Certificate authorized by the U.S. Grain Standards Act) will be provided to both parties.<sup>1</sup>

The quantity of organic commodity delivered could also be manipulated through quality determinations. For example, the contract might require a premium price for any bushels in excess of 75 bushels. Let's say the farmer delivers 100 bushels. Based on the contract, the farmer would expect a premium price for the 25 extra bushels. However, a buyer who is not interested in paying for that many bushels might argue that quality problems with the delivery bring the useable quantity below 75 bushels, and therefore no premium price is applicable. For an in-depth discussion of quality standards and organic contracts, please see pages 6–20 through 6–29 of this chapter and Chapter 12, pages 12–26 and 12–27.

Finally, handling practices for commodities such as grains, beans, and seed might allow the buyer to manipulate quantity by increasing the stringency of cleaning procedures, as discussed below.

### **Does the contract require cleaning or “cleanout”?**

If the contract requires cleaning of the product, be sure that the contract clearly answers the following questions:

#### **Who Pays for Cleaning?**

If cleaning is required, the contract should clearly state who is responsible for the cleaning costs. If you are required to pay for cleaning, make sure to factor that cost into your overall profit calculation.

**Example: Producer Must Pay for Cleaning of Commodity**

Any cleaning and/or processing required to remove foreign material from delivered commodity shall be conducted by Buyer at Producer's expense.



Cleaning provisions often require the farmer to pay for cleaning but place no cap on the total cost the farmer could be charged. Be wary of contract language that gives the buyer too much discretion over how much the buyer could charge you for cleaning.

For example, if you agree to pay for “all costs buyer incurs related to the cleaning required for commodity to meet quality standards,” you could end up responsible for a large sum. This is so because: (1) you cannot control the costs of the cleaning process; (2) you cannot control the wage paid to workers for the cleaning; and (3) costs “related” to the cleaning is a very broad category, allowing costs that might not be directly part of the cleaning process.

**Better Examples: Cleaning (Buyer Pays, Price Cap)**

The cost of cleaning shall be borne by the Buyer and shall not be deducted from the price paid to Producer.

**Or:**

The cost of cleaning shall be borne by the Farmer, but no more than the actual cost of cleaning incurred by Buyer, or \$.50 per bushel, whichever is less.



**Who Takes the Loss if the Organic Product Is Damaged During Cleaning?**

Ownership during cleaning will likely determine who takes the loss if the organic product is damaged during cleaning. If the farmer owns the product during cleaning, and the product is damaged, the farmer could



suffer significant losses. Thus, you may wish to negotiate a contract provision stating that the buyer bears the risk of loss for damage to organic product during cleaning, meaning that the buyer cannot charge you for any damages caused by cleaning processes.



Example: Buyer Bears Risk of Loss During Cleaning and Other Handling

Buyer shall bear the risk of loss for any damage to the organic product that occurs during cleaning, processing, storage, or other handling activities conducted by Buyer.

How Clean Is Clean?

It is important to know how thoroughly the buyer will clean your commodity. This is important because if two buyers offer the same price for a bushel of grain, but one buyer has a higher standard for what “clean” means, you could end up with a smaller payment from that buyer because the amount of cleaned product will be smaller.

Think about whether you could use the contract to help control the level to which your product is cleaned. For example, the buyer could agree to allow you to be present to observe the cleaning process. Alternatively, if the cleaning process is mechanical, perhaps you and the buyer could agree on settings for the machines. Or, the contract could set out that you will test the product before delivery and that cleanout dockage will be no more than test results indicate.

In a variation of the situation described above, be cautious if one buyer is offering a significantly higher price than all of the other buyers. That buyer might be attempting to attract farmers with the high price, but might also have a much higher cleaning standard, meaning farmers will not end up receiving the benefit of the advertised higher price. Consider asking other organic farmers who produce similar commodities about their experience with your potential buyer.

Will the Buyer Clean Instead of Rejecting?

One way cleaning could operate in the farmer’s favor is if the farmer can negotiate a provision allowing cleaning of a low-quality product in place

of rejection. Instead of an all-out rejection if a delivery fails to meet quality standards, the buyer could agree to be responsible for cleaning the product to raise the quality (assuming this is possible, such as for some grains, beans, and seeds). However, if the farmer agrees to pay for cleaning that will be arranged for or performed by the buyer, it is advisable to set a price limit for the cleaning.

To put a limit on possible cleaning costs, the farmer could agree that the buyer will clean a low-quality delivery to higher quality standards in place of outright rejection, but that the cost will be no more than a certain dollar amount per pound, bushel, ton, or another unit of measurement. In this way, the costs the farmer could incur are limited by the quantity delivered, which gives the farmer more control over how much might have to be paid for if cleaning becomes necessary.

**Example: Cleaning in Lieu of Rejection**

If the contracted crop falls below quality standard outlined herein, Buyer may reject, or, in Buyer's discretion, deduct the costs related to cleaning the crop so that it meets quality standards, and to reduce the purchased quantity of the crop by the amount of cleanout resulting.



**Example: More Limited Cleaning in Place of Rejection**

If necessary, Buyer may clean the delivered crop to meet quality standards outlined herein. If significant cleaning is necessary, Buyer will obtain Seller's permission before proceeding to clean the crop. However, Seller will receive a \$1.00 per bushel deduction for any cleaning services performed by Buyer.



**Who Owns the Cleanout?**

The contract should also clearly state who owns the “cleanout.” “Cleanout” is the portion of the delivery that is removed during the

cleaning process and can be quite valuable. If the farmer owns the cleanout, the farmer may be able to sell the cleanout directly to the buyer because it can often be further cleaned, leaving a small portion of higher-value commodity.

Farmers who could profit from cleanout should address cleanout in their contracts. It could be helpful to include language stating:

- Who owns the cleanout.
- Whether there is an option for the buyer to purchase the cleanout.
- Whether the buyer agrees to purchase the cleanout and at what price.

Additionally, it is important to confirm that the cleanout will remain an organic product, and to require that all cleaning activities be conducted in certified organic handling facilities.

Some cleaning methods might damage the cleanout to the point that it is no longer saleable. If you are worried about this, you could negotiate contract language requiring the buyer to either maintain the cleanout in saleable condition to be returned to you or to purchase the cleanout (regardless of condition) at a mutually agreeable price. Alternatively, the buyer could agree to use a different cleaning process that would not damage the cleanout.

**Better Examples: Cleanout**

Grower shall own cleanout. However, Buyer reserves the option to purchase cleanout at 30 percent of the contract price. Buyer agrees to maintain cleanout in a saleable condition, and further agrees to maintain cleanout as a certified organic product. If Buyer does not exercise option to purchase cleanout, Buyer shall return cleanout to Grower in good condition.

Or:

Buyer agrees to bear reasonable cleaning costs and to purchase cleanout at a price to be agreed. If the parties cannot agree on a price, cleanout shall be returned to Grower in saleable condition.

**Does the contract include a utilization clause or a quota option?**

Utilization clauses and quota options will likely apply only to contracts for organic milk.

Utilization clauses state that a farmer will be paid different prices based on the percent of organic milk sold in the organic or conventional markets. For example, a buyer might pick up 20 cwt of a farmer's organic milk. The farmer will not know what price will be paid for that milk until the buyer attempts to sell the milk into the downstream milk market (that is, to a processor). At the end of the day, the buyer may be able to sell 75 percent of the farmer's milk as organic, but may end up selling 25 percent of the milk as conventional milk. In this scenario, under a utilization clause the farmer will receive an organic price for only 75 percent of the 20 cwt (15 cwt) and will receive the lower conventional price for the remaining 25 percent (5 cwt).

Quota options allow buyers to put a cap on the amount of product they will accept from farmers (even if the buyer normally purchases farmer's entire production). In an oversupplied market, such as during the 2008-2009 organic milk surplus, quota options allow buyers to avoid being locked in to purchasing farmers' entire production.



**Quota options are generally less harmful to organic dairy farmers than utilization clauses, especially if:**

1. The buyer agrees to provide the farmer with enough notice before exercising the quota option so that the farmer can decrease production, and
2. There is a floor level below which the quota cannot be set and which is acceptable to the farmer, and
3. The buyer agrees that the farmer can use milk in excess of the quota in any way the farmer chooses, such as making cheese or using the milk as fertilizer.

Utilization clauses are risky because the farmer cannot control the buyer's sales efforts, and because it is hard for the buyer to keep track of exactly how one farm's milk is used when there is so much commingling of milk during bottling and processing.

If you must agree to a utilization clause, try to negotiate language that limits your exposure. For example, you could agree that for any given period, the buyer must pay the organic price for at least a set percentage of the milk delivered (for example, 85 percent).

## QUALITY

### **What are the quality requirements?**

Quality issues can be some of the most contentious in any farmer-buyer relationship. This can be especially true for organic farmers and buyers because organic integrity is taken so seriously in the organic market. Organic products are “credence goods” (also known as “trust goods”). Credence goods have attributes that buyers cannot directly evaluate. Instead, buyers must trust that the farmer has followed organic production practices; it is difficult or impossible to determine the integrity of an organic farm product simply by examining the product or even by testing it.<sup>2</sup>

Disputes over product quality generally occur when the buyer and the farmer do not agree about either how quality will be tested or what the test results mean. Consequently, clearly defining the quality requirements and the quality determination process can help prevent quality-related contract disputes.

Note that some buyers might require written documentation related to quality and organic integrity in connection with deliveries of organic farm products. See Chapter 7, pages 7–9 through 7–12, for a discussion of documentation related to organic commodities.

### **Is quality measured using objective standards?**

Buyers generally assess the quality of organic farm products by evaluating certain criteria—such as color, size, weight, protein levels, brix, moisture, somatic cell count, etc. Although there are a wide variety of criteria for evaluating organic commodities, every organic farmer can assess the criteria that will be used for their product by looking for one element: objectivity.

If organic quality criteria are measured by “objective” standards, the standards exist independently of individual perception or preconceptions. Put another way, when measuring a certain criterion (for example, weight) using an objective quality standard, two individuals conducting separate measurements of the same commodity would be expected to reach the same conclusion.

An example of contract language that measures quality using an objective standard could be, “All cucumbers delivered must be at least 5 inches in length.” Here, the quality criterion is length, and the standard is a set number of globally recognized units of measurement (inches). Thus, if a farmer and a buyer separately measure the same cucumber, they are likely to reach the same decision as to whether the cucumber is at least 5 inches long.

In contrast, an example of contract language that measures quality using a standard that is not objective could be, “Buyer will only accept delivery of ‘large’ organic cucumbers.” This standard is not objective, because two people assessing the same cucumber could easily come to different conclusions about whether the cucumber is actually “large.” The meaning of “large” is not tied to any objective measurement; it is instead a highly unpredictable subjective assessment tied to individual perception.

### **Aim For Objective Quality Standards**

Objective quality standards are important for farmers because buyers often test quality outside the farmer’s presence. Objective quality standards make the quality assessment process more predictable for the farmer.

Therefore, if the organic contract does not measure quality using objective standards, consider negotiating for more objectivity. If the quality measurements for your organic farm product are inherently subjective, or if the buyer is unwilling to agree to an objective standard, consider negotiating contract language that allows you to be more involved in the quality testing process.



### **Who will conduct the quality test?**

It is important to think about who will be conducting the quality assessment (the farmer, the buyer, or a third party). The person who conducts the quality assessment often has significant control over the outcome. Consequently, a farmer might understandably be concerned if a buyer has total control over weighing, grading, testing, or cleaning the farmer’s organic farm products, because the assessment might be more likely to favor the buyer. You might be even more concerned about your buyer having total control over the quality assessment process if the

quality criteria are hard to measure or the criteria are measured using standards that are not objective. At the end of the day, quality assessments often have a big impact on how much money farmers earn under organic contracts.

If the buyer is conducting the quality test, as is often the case, it is most important to try to negotiate objective quality standards, as discussed above. In addition, try to include contract language that will act as a “check” on the buyer’s total control over the quality assessment. For example, the farmer and the buyer could agree that the assessment will be conducted in the farmer’s presence. Or, the farmer could agree that the commodity will be weighed or graded by an independent third party. The contract could also create a quality dispute resolution process if the parties cannot agree on a fair assessment (see page 6–25 of this chapter).

In sum, it is possible to design a quality assessment process that does not give the buyer total control. You can be creative in negotiating a solution that works best for your situation and particular organic commodity.

### **Are the quality testing conditions clearly defined?**

In the organic contract context, quality testing can present a number of issues for farmers. However, many difficulties can be prevented if the farmer and the buyer clearly spell out the conditions of quality testing in the contract.

#### **Will the Test Be Conducted by the Farmer, the Buyer, or a Third Party?**

Usually, farmers will not be conducting quality tests. Independent third-party lab tests are also relatively uncommon as a first test due to their expense. Thus, if the buyer is conducting the quality test, as is typically the case, consider whether you wish to negotiate protections to ensure testing fairness.

For example, you may wish to negotiate language stating that quality testing must be conducted by someone who has experience in using the necessary test and who will follow proper testing protocol. User error is a concern for all tests, but it is even more of a concern outside of a laboratory setting. For example, GMO strip tests can be compromised if they are conducted without proper procedures, such as being performed in windy conditions or too close to known GMO crops. If the person conducting the test fails to observe proper procedures, you could end up with an unwarranted rejection that could be both costly and time-consuming.



### Who Will Pay for the Test?

Quality testing can be a significant expense, especially if the test samples are numerous or multiple tests are needed. Therefore, it is recommended that the contract specifically state whether the farmer or the buyer will bear testing costs. Some organic contracts require the buyer to pay for any initial testing, but may shift all or part of the cost burden to the farmer if the farmer requests independent third-party testing for any disputed test results.

### Where Will the Test Be Performed?

Quality testing can be performed at a variety of locations, including the farm, the delivery site, the buyer's facility, or a laboratory. From the farmer's perspective, it might be most desirable to test at the farm, where the farmer can better supervise testing and the organic commodity has less exposure to contamination. However, if the buyer will not agree to test at the farm, you may wish to negotiate contract language that requires the buyer to test under certain conditions, such as in a sterile environment or away from non-organic and GMO commodities.

### When Will the Test Be Conducted?

As mentioned above, from the farmer's perspective, it may be most desirable to quality test the commodity before it leaves the farm. The second best option is to perform testing as soon as possible after the shipment leaves the farm. In general, the longer the organic product has been away from the farm, the more opportunity there is for contamination, commingling, physical damage, spoilage, etc. Timeliness is especially important for perishable goods like produce and meat. Furthermore, it is risky to allow any test for contaminants like GMOs or pesticides to occur after cleaning or processing because the machinery used in those processes could be the source of contamination.

Consider placing a specific time limit on any required quality testing, either measured in units of time (hours, days) or in relation to stages of production (immediately upon delivery, prior to processing, etc.).

### What Are the Test Criteria?

The contract should state exactly what quality criteria (for example, moisture, protein, somatic cell count) or contaminants (such as GMOs or pesticides) are being measured by the test. The contract should also clearly state the level above which (for contaminants) or below which (for desired traits) the delivery will be rejected and any other important measurement levels related to test results, such as premium or discount

levels for various qualities or contaminants. It is risky not to clearly set out rejection, premium, and discount levels in the contract.

### What Test Documentation Is Required?

You may wish to negotiate contract language requiring the buyer to send you documentation of any quality test results. You might also require documentation of the testing process itself, through real-time photography, video, or other means.

### **Does the contract require you to take product samples?**

If the organic contract requires you to take samples, make sure you understand exactly how many samples should be collected, what size they should be, how they should be packaged and labeled, where and when they should be taken, and whether the samples must be shipped to the buyer or a third party. Be sure to clarify any uncertainties in the contract language before signing.

You might be required to send a sample to the buyer and receive approval before delivering your organic commodity. Consider keeping “copies” of all samples you send (that is, additional samples taken at the same times from the same locations).

#### Example: Farmer Required to Submit Product Sample

Seller agrees to deliver a representative five-pound product sample from each storage unit within a reasonable time after harvest. Buyer will test samples immediately upon receipt. Samples must be clearly labeled with Seller's identity, lot number, and the number of storage units per lot.



**Always Take Samples for Yourself**

Even if the contract does not require you to submit samples, it is always smart to keep samples of your organic commodity for yourself. Maintaining reliable samples can help you prevent or settle a quality dispute with the buyer, as can good recordkeeping and photographs.

**Is there a quality dispute process?**

It can be extremely helpful to have a contract provision detailing what will happen if you disagree with the results of the buyer's quality assessment. For example, if the buyer receives a delivery of your organic farm products and claims that the quality is below the standard required in the contract, can you dispute this assessment? If so, how would you and the buyer resolve the dispute?

Think about whether, if a dispute occurs, you and the buyer might wish to identify a third party (such as a laboratory or an independent expert in the particular organic commodity) who could conduct a "tiebreaker" quality assessment. You and the buyer could agree to abide by the results of the third party's test. It is important, however, to choose a third party that both you and the buyer trust to be independent and neutral. Also consider agreeing in advance how a third-party quality assessment will be paid for.

**Example: Independent Laboratory Testing**

Should a quality discrepancy or dispute arise between the parties regarding a particular sample or delivery, either party can request the sample be tested by an independent, qualified laboratory. The parties shall bear the expense of the test equally.

### Access to Samples

In addition to keeping your own duplicate samples, as recommended above, you may wish to negotiate contract language that allows you to have access to any samples that the buyer determines to have “failed” the quality test. You can then perform your own quality test on those samples, or send them to be tested by an independent third party. Make sure to keep good records of any tests that you conduct.

### Timing of Quality Issue Notifications

Consider setting time frames within which: (1) the buyer must notify the farmer that the buyer believes there is a quality issue, and (2) the farmer must dispute the buyer’s quality assessment. Ideally, the buyer would notify the farmer shortly after delivery, and the farmer would have a reasonable amount of time to dispute the buyer’s quality assessment.

### Keep Your Product Separate While a Quality Dispute Is Ongoing

Consider including contract language requiring the buyer to keep your product separate from the other farmers’ products while a quality dispute is ongoing. This is most applicable to crops that are often mixed with other farmers’ products during shipment, storage, processing, or other handling (such as grain or milk). It is very difficult to dispute a test result you do not agree with if your product cannot be identified.



**Example: Quality Testing and Dispute Resolution**

Buyer shall conduct quality testing inside Buyer's facility within two business days of delivery. Buyer shall notify Grower of any test results within one business day of testing; Grower shall be allowed three business days to object to test results. If Grower objects, Buyer may retest once and/or send samples to XYZ independent third-party laboratory for a final test. Grower and Buyer agree that the laboratory test results shall be final.

Grower and Buyer shall bear the cost of laboratory testing equally, and Grower shall have access to test samples at all times. Buyer shall maintain the integrity of Grower's delivery until such time as any quality dispute is resolved.

**What are the consequences of poor quality?**

It is important that the consequences of delivering low-quality product be clearly spelled out in the organic contract. In addition to helping the farmer decide whether the contract is worth signing, detailing the exact consequences of poor quality will give both parties certainty as to what will happen if quality falls below contract standards.

One of the most common consequences of a low-quality product is buyer rejection. It is helpful for the contract to state whether a delivery, if rejected, must be rejected in its entirety, or whether the buyer has the option to accept a portion of the delivery and reject the rest.

Additionally, the contract should set a specific time frame for buyer rejection. Be careful with contracts that use vague language to describe the time frame for rejection—like “reasonable” or “acceptable.” This is especially important if the organic commodity must be rejected in a short period in order to allow for potential resale (such as for perishable commodities), or if you are worried about contamination or infestation occurring at the buyer's facility.

**Example: Rejection for Failure to Meet Quality Requirements**

After a reasonable time for inspection and evaluation of the conformity of product to the minimum quality requirements stated herein, Buyer shall have the option to reject either the entire shipment or a portion of the shipment. In the event of material nonconformity, Buyer may also declare the contract null and void.



Consequences of poor quality can also include:

- dockage or discounts,
- a requirement that the farmer refund payments the buyer has already made,
- a requirement that the farmer reimburse the buyer for the costs of shipping and handling the rejected product when sending it back to the farmer, or
- a requirement that the farmer compensate the buyer for the cost of obtaining replacement organic product.

Consider how these requirements could cut into your potential profits and whether they make the contract too risky for you to sign.

Some organic contracts require the buyer to provide a written explanation of reasons for rejection or evidence of the basis for rejection (for example, photographs or test results). This kind of provision can provide farmers some protection against baseless rejection.

**Who is responsible for poor quality?**

Organic contracts often include a statement that the farmer is wholly responsible for the quality of the organic product, and that the buyer cannot be held liable for the farmer's inability to meet contract standards. This kind of statement may sound reasonable on its face, but might not be fair if the quality is not tested until the organic commodity has been in the buyer's control for some time. Consider negotiating language changing such a statement to include a limitation on the farmer's responsibility

once the commodity has passed into the buyer's control. See Chapter 7 for a discussion of ownership, liability, and control during the transportation and processing stages.



Example: Shifting Risk of Loss to Buyer Upon Delivery

Seller bears risk of loss and responsibility for quality of the organic product under contract up to the moment of delivery at Buyer's facility; at that time the risk of loss shifts to Buyer.

**CHAPTER 6 — ENDNOTES**

<sup>1</sup> See 7 U.S.C. §§ 71-87 (2012).

<sup>2</sup> See Miriam Berges and Karina Casellas, *Quality Warranties and Food Products in Argentina: What Do Consumers Believe In?*, at 4 (International Association of Agricultural Economists Conference, 2006), available at <http://ageconsearch.umn.edu/bitstream/25526/1/pp061249.pdf> (noting the existence of a market for credence or “trust” goods is either made possible by: (1) the reputation of the seller; or (2) a third-party quality guarantee, “often in the form of a regulation which provides consumers with a substitute for the information and trust they lack”).



# 7 Transportation, Delivery & Storage

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## CHAPTER QUICK TIP

### **Limit Your Obligation to Prevent Contamination**

Contract language stating you will take “all measures” to prevent contamination could require you to take extremely expensive measures. Instead, you can limit your obligation to prevent contamination by substituting language stating you will take all “commercially reasonable” anti-contamination measures, or that you will use “best efforts” to prevent contamination.



# TRANSPORTATION

## Who is responsible for transportation?

It is a good idea to ensure that the contract clearly defines how the organic product will be transported to the buyer, as transportation can be both complex and costly.

You may wish to include contract language covering the following issues:

### Who is Responsible for Arranging Transportation?

Either the farmer or the buyer could be responsible for arranging transportation. If you make the arrangements, you will have more control over who is hired and the specific transportation services requested. On the other hand, making transportation arrangements will require you to expend time and resources that you would not have to expend if the buyer had the responsibility.

Whether it is more favorable for the farmer or the buyer to arrange transportation will also depend on who is paying for transport, which is discussed on the next page.

- *Be careful with transport companies that may not understand the needs of organic farmers*



If you are arranging transportation for your own products, be sure that transportation company personnel are fully informed about the contract obligations involved and exactly how and when the delivery must take place to prevent violation of the contract. It's a good idea to discuss the specifics with transport company office employees, as well as on-the-ground transport company employees (such as drivers).

In a best-case scenario, you will also enter into a separate contract with the transportation company. If the company agrees to ensure that your organic commodity is transported on time, safely, and without contamination, the company will likely be liable to you for any damage caused during transit. Be aware, though, that some trucking companies have standard insurance policies

covering damage to the product during transport that may not reflect the organic premium. You may wish to check with the transport company regarding its insurance.

Please see pages 7–12 through 7–16 of this chapter for a more thorough discussion of contamination prevention during transit.

- *Significant changes proposed for transport of bulk, unpackaged organic products*



In July 2011, the National Organic Program (NOP) published a draft guidance concerning the handling, including transport, of bulk, unpackaged organic products. The proposed policy would require handlers of unsealed organic products to be certified organic or be specifically named in the farmer's or buyer's organic plan and be subject to inspection. If the requirement is not satisfied, the proposed policy would result in loss of organic status for the commodity. The policy, if adopted, is likely to make arranging for transport of bulk, unpackaged organic products more complicated and probably more expensive. However, it could also help better protect organic integrity from farm to table.<sup>1</sup>

A public comment period on the draft guidance was open until April 3, 2012. At the time this guide was printed, it was not known when or whether NOP will adopt these proposed handling rules as a program requirement.

#### Who Pays for Transportation?

For some organic commodities, like organic milk, the cost of transportation was historically the buyer's responsibility. In recent years, however, some buyers have begun charging farmers significant "hauling fees." Whether you are sharing the burden of transportation costs or are bearing the costs on your own, be sure to factor that cost into your expected profit calculation.

**Note for Organic Dairy Farmers**

Milk hauling fees have traditionally been flat fees (either per year or per month). However, some organic milk buyers have changed their contracts to include hauling charges based on the farm's distance from the milk processing plant. Consequently, organic dairy farmers should pay close attention to the details of any milk hauling charges in current contracts.

As a general matter, one party to the contract might be responsible for both arranging and paying for transportation—or the duties could be split between the two parties. If the duties are split, one party will likely pay all of the transportation expenses up front and then be reimbursed by the other for all or part of the expenses. If you have a reimbursement arrangement with a buyer, it is a good idea to set a deadline for reimbursement payments. You may also wish to set out whether there are any restrictions on reimbursement. For example, is there a limit on the amount of reimbursement for transport regardless of actual cost? Will reimbursement apply to partial loads? If the shipment does not fill the truck, rail car, or other vessel, and the transport company charges for the entire vessel, which party has to pay for the unused space?

**Can the Transportation Payment Structure Change During the Contract?**

Some organic contracts state that although the buyer might initially cover transportation costs, the buyer retains the right to begin charging for transportation (with or without notice). At present, this issue is most common in organic dairy contracts. Transportation costs can be significant, and this kind of provision allows buyers to shift significant expense to farmers with little or no notice. Therefore, it is best to avoid this kind of provision. However, if it cannot be avoided, a compromise could be to try to negotiate reasonable notice and/or a limit on farmer-covered transportation costs. At the very least, however, farmers who sign contracts that allow for increased transportation costs during the contract should try to factor a reasonable increase in transportation costs into their cost-benefit calculation before signing the contract.

**Is a Specific Type of Transportation Required?**

Does the contract require that a particular type of transportation be used (truck, rail, air, etc.) or a particular freight service? Or, does the contract require certain transport characteristics, such as refrigerated shipping

(perhaps at a certain temperature with a temperature recorder) or the maintenance of certain moisture levels?

If you are arranging and/or paying for transportation, it may be to your benefit if the contract allows flexibility in the type and characteristics of transportation used—while still maintaining quality.

### **Are there any packaging requirements?**

Organic contracts are often quite specific when it comes to packaging the organic commodities for shipment. However, if the contract does not contain packaging requirements, consider whether adding specific requirements might be helpful in preventing future buyer complaints. It is more difficult for the buyer to complain about issues related to packaging (such as damage or contamination during transit) if you have agreed upon packaging requirements at the outset. Still, it may be to your benefit to retain flexibility in packaging options. You could strike a balance by identifying a range of acceptable packaging options in the contract.

#### **If the Contract Does Discuss Packaging, You May See Contract Language Related to the Following:**

- *Type of packaging*

The contract may call for a certain type of material or container, such as: bags (plastic, paper, mesh), bins (metal, plastic, wood), boxes (cardboard, wood, plastic), etc. Additionally, the contract may require packaging capable of maintaining the organic products at a certain temperature.

- *Size of packaging*

The contract may require specific packaging dimensions. This requirement will likely be designed to ease delivery and/or organization within the buyer's facility (for example, a 42-inch by 48-inch plastic pallet, or a one-ton storage bin) or sales (for example, 50-pound plastic bags may be the standard for selling an item in the wholesale market).



Example: Packaging Requirement

Required Packaging. All products must be shipped in new 25-lb clear 2-mil re-closable plastic bags.

- *Quality of packaging*

The contract may also include requirements relating to packaging quality. The requirements may be vague, requiring materials that are, for example, “clean and in satisfactory condition.” Or, quality requirements may be more specific, requiring plastic bags of a certain thickness or standardized pallets from a particular supplier. The contract might require brand-new packaging or might allow used packaging in good condition.

Consider whether you could benefit from more clarity in the contract regarding packaging quality or whether vague specifications give you useful flexibility.

- *Labeling*



Many organic contracts require farmers to label their commodities with the words “Certified Organic.” If you do label your commodities as organic, note that, if you are shipping or storing raw or processed agricultural product in non-retail containers labeled as containing organic ingredients, NOP regulations require those non-retail containers to be labeled with the production lot number of the organic product.<sup>2</sup>

### **Production Lot Numbers**

Production lot numbers are unique codes associated with individual operations. As such, they often play a critical role in the identification of an organic product as it moves through the organic food system. Some buyers may be interested in tracking organic farm products by farm, barn, field, parcel—or even by bed. Production lot number systems can allow this level of tracking. Moreover, even if the contract does not require production lot numbers, NOP regulations require them for non-retail containers labeled as containing organic ingredients.

An example production lot number might include the farmer name, the type of crop, storage unit or field number, and the production date. For example, the lot number for Farmer Jane Smith's organic soybeans harvested on September 28, 2012 and stored in bin #5 might look like: 092812OS5Smith. To be effective, production lot numbers must be used consistently once established.

Creating and maintaining a labeling system that links products to units of production can be time-consuming and potentially somewhat costly, so be sure to factor any labeling costs into your contract cost-benefit analysis.



Labeling requirements in organic contracts other than the production lot number vary widely, and could include information like your farm's name, type of organic commodity, weight, lot number, test results, GMO-free status, or other identifiers.

The NOP regulations expressly allow non-retail containers used only to ship raw or processed organic products that are labeled as containing organic ingredients to display:



- Name and contact information of organic certifier (ACA)
- “Organic” designation
- Handling instructions to maintain organic integrity
- NOP seal
- Organic certifier (ACA) seal<sup>3</sup>



The production lot number, if applicable, must be displayed.<sup>4</sup>

The NOP regulations do not prohibit non-retail shipping or storage containers from displaying information in addition to those items listed above.<sup>5</sup>



**Example: Labeling Requirement Provision**

Labeling: Producer shall clearly label the outside of each bin with the Producer's assigned control number; year of harvest; variety name; weight; and the words "Certified Organic." The words "Certified Organic" shall also appear on the Bill of Lading and any other accompanying documentation.

If the contract requires that you invest in special packaging or satisfy elaborate labeling requirements beyond NOP regulations and other requirements imposed by federal labeling laws, consider whether you can afford the expense. If not, consider negotiating an alternative packaging solution.

Farmers should be aware that federal laws other than the NOP regulations may impose additional food labeling restrictions and requirements that are beyond the scope of this guide. The National Agricultural Law Center website contains a section dedicated to food labeling law that may be helpful and is available at:

<http://www.nationalaglawcenter.org/readingrooms/foodlabeling>.<sup>6</sup>

**Will the buyer provide packaging?**

Once a farmer knows what type or types of packaging are required under the contract, the next consideration is where to obtain packaging. Sometimes buyers will provide the packaging materials or require farmers to purchase packaging materials from the buyer. If a farmer is making numerous deliveries throughout the course of the year (such as organic milk or eggs), the buyer might offer a packaging materials exchange. In this type of arrangement, the farmer delivers the packaged commodities and picks up empty packaging in exchange for the packaging containing

the delivered commodity. If the buyer does not provide packaging, the farmer will have to find a packaging supplier.

Although it might be more convenient if the buyer provides packaging (or selects packaging for you to purchase), you might have the following concerns:

#### How Much Will the Packaging Cost?

If the buyer selects the exact packaging materials the farmer must purchase, the farmer loses the opportunity to shop around or find a better deal on packaging. The farmer may also end up paying a premium to the buyer. Consider more flexible contract language, such as “the seller may purchase packaging from the buyer,” which gives you the opportunity to purchase packaging materials from the buyer if it is convenient and advantageous, but allows you the freedom to look for a better deal.

#### Example: Seller Purchase of Packaging from Buyer

Seller may purchase the following items from Buyer, as they are available: plastic or hardwood pallets; other packaging material and supplies; labels; temperature gauges; and other packing supplies. These items must be paid for within 30 days.



#### Will the Packaging Materials Be Thoroughly Cleaned and in Good Condition?



The assurance that any packaging provided by the buyer will be clean and in good condition is particularly important for organic commodities, and should be set out in the contract. The NOP regulations prohibit the use of packaging materials and storage containers that contain synthetic fungicides, preservatives, or fumigants. Additionally, the regulations prohibit the use or reuse of any bag or container that has been in contact with any substance that would compromise the organic integrity of any organically produced product placed in those containers, unless such reusable bag or container has been thoroughly cleaned and poses no risk of contact between the organically produced product or ingredient and the prohibited substance.<sup>7</sup> Therefore, if buyer-

provided packaging or storage materials are not appropriately cleaned, you may be in violation of the organic rules.

Also, does the contract protect you if buyer-provided packaging contaminates your products and the contaminated shipment cannot be marketed as organic? Must the buyer still pay for the contaminated products at the contract rate, do you take a loss on that shipment, or is there another result?

If the buyer-provided or buyer-mandated packaging is not in satisfactory condition (such as, splintered wooden pallets, rusty bins), does the contract protect you? Consider including contract language stating that the buyer will provide packaging materials in satisfactory condition and will replace any unsatisfactory materials promptly and free of charge. Alternatively, the contract could state that you have the right to purchase alternative packaging and be reimbursed for its cost if the packaging provided by the buyer is not in satisfactory condition.

#### Will the Materials Be Provided in a Timely Fashion?

Timely availability of packaging materials is especially important for perishable organic commodities. If you are required to wait for buyer-provided packaging, the delay could cause spoilage. You may wish to negotiate language stating that, if a delay occurs in packaging being provided (including the packaging being dirty or otherwise unusable), the buyer will protect you from any consequences of the delay. This could include the buyer's waiving quality standards for the shipment or compensating you for replacement packaging and/or the cost of products that spoiled due to the delay.

#### **What kind of documentation is required as part of the organic shipping process?**



Organic contracts often require documentation of organic status. Make sure you are prepared to provide required records at the appropriate time: when the contract is signed, prior to shipping, with the shipment, or after shipment. Also, check to see whether you must pay a fee to obtain any necessary documents and how much time it generally takes to obtain required documentation. For example, you may have to wait and/or pay a fee for documents that must be obtained from your organic certifier, such as an organic transaction certificate or a TM-11 form (both discussed below).

Although the Contract May Require Additional Documentation, Some Commonly Required Documents Include:

- *Audit trail documents*
  - Sales invoices or other delivery papers representing a complete record of the transaction
  - Inventory and shipping logs
  - Product sales records
  - Records of contracted custom application or harvest
  - Scale tickets or weight slips
  - Clean transport affidavits (discussed in the next section)

- *Bills of lading*

A bill of lading is the official document prepared by the transport company accepting the goods for shipment. It details information such as the item, quantity, lot number, value, vessel details, date, port, seller, buyer, terms of delivery, etc. The contract might require that the bill of lading state that the products are certified organic or that the product was loaded at a certain temperature.

- *Copy of farm's organic certificate*

This type of certificate simply documents the trade of certified organic products. Organic certificates are issued by your farm's organic certifier. While the original certificate is covered by the certification fee, you may have to pay for additional copies or transaction certificates. The certificates can be used for both domestic and international sales.

- *GMO-free documentation*

Please see Chapter 8 for a thorough discussion of GMO-related issues, including documentation.

- *Testing certifications*

The contract might require your organic farm products to be tested prior to shipment and might further require you to provide documentation of the test results. One common example is a USDA Phytosanitary Certificate, which certifies that fresh fruit and vegetables are healthy and pest-free. This certificate is generally issued by the U.S. Animal Plant Health Inspection Service (APHIS) or another federal or state government agency.

- *International documents*

International sales of organic commodities require particular documentation. The type of document required will depend on the country of export and the type of commodity. Some commonly required international certifications include the following:

- USDA Export Certificate (TM-11) for Japan and Taiwan
  - The United States has export arrangements with Japan and Taiwan stating that USDA-certified organic products exported to these countries must be accompanied by export certificate form TM-11 that verifies that the product complies with the terms of the export arrangements.<sup>8</sup> Only organic certifiers can issue TM-11 export certificates. Thus, farmers whose contracts require this certificate will have to coordinate with their certifier and may have to pay a fee.
- Attestation for Export to Canada
  - As of 2009, the United States has an organic equivalence arrangement with Canada, meaning that organic operations certified to NOP standards (or to Canada Organic Product Regulation (COPR) standards) may be labeled and sold as organic in both the United States and Canada.
  - The following statement must accompany products produced under the US-Canada Organic Equivalence Arrangement: “Certified in compliance with the terms of the US-Canada Organic Equivalence Arrangement.” This statement must appear on documentation traveling with the shipment. The statement may be included on the organic certificate, a transaction certificate, bill of lading, or purchase order.<sup>9</sup>
  - For products packaged for retail sale, labels or stickers must state the name of the U.S. or Canadian certifying agent and may use the USDA Organic seal or the Canada Organic Biologique logos. Wholesale products only require lot numbers.
- European Union Certificate of Inspection
  - As of June 1, 2012, certified organic products from the United States can be represented as organic in the European Union (EU). U.S. organic products exported to the EU must be accompanied by an EU organic import

certificate completed by an NOP-accredited organic certifier. Organic certifiers must provide the signed certificates of inspection (also called EU import certificates) to the farmer so that the certificate may travel to the EU with the organic product.<sup>10</sup>

- Tariff classifications
  - In 2011, U.S. tariff classifications were established for organic products to ease tracking of imported and exported organic products throughout the world. These so-called “Schedule B codes” are required when submitting export shipment data or documentation.

It is important to know what documentation is required so you can be sure to provide the appropriate documents necessary to prove and maintain organic certification. You may wish to negotiate for your buyer to cover the cost of any documentation or to handle the process of obtaining documentation. It may also be helpful to know what consequences might follow from any failure to provide correct documentation in a timely fashion. Will the buyer reject your delivery? Will the buyer delay acceptance of your delivery until the appropriate records arrive? On the other hand, some contract obligations related to documentation requirements might be formalities your buyer is willing to waive during contract negotiations (although others are legally required and non-waivable).

To download blank forms related to shipping of organic products, including many of those listed above, visit [www.attra.org](http://www.attra.org), and click on “Help Tools & Blank Forms.” Another helpful online resource is the Iowa Organic Certification Program website, <http://www.iowaagriculture.gov/AgDiversification/organicCertification.asp>.

### **How does the contract address contamination prevention during transport?**



Transportation of organic products currently represents a hole in the NOP regulations. Farms must be certified organic, and processors must be certified organic—but trucks, trains, and other forms of transportation currently cannot be certified organic. Although this may change if the proposed bulk handling policy discussed earlier in this chapter is adopted, for now farmers and buyers are left to create their own system to prevent transportation-related contamination. Even so, many organic

contracts do not sufficiently address the special considerations for transporting organic products.

Consider whether the contract satisfactorily addresses the following issues:

- *Who is responsible for preventing transport-related contamination?*

Is it the farmer's responsibility, the buyer's responsibility, or the transport company's responsibility to prevent contamination during transport?

If the buyer takes responsibility for preventing transport-related contamination, make sure the organic contract expressly states that the farmer has no liability for contamination during transit, that the buyer will cover all losses caused by contamination, and that the farmer will suffer no losses as a result of failure by the buyer or the transport company to prevent contamination.

If the farmer is arranging for transport with a transport company that agrees to take responsibility for transport-related contamination, the farmer's separate contract with the transport company should contain the assurances mentioned above (that is, the farmer has no liability for contamination during transit, the transport company will cover all losses caused by contamination, and the farmer will suffer no losses as a result of failure to prevent contamination).

- *Who pays for contamination prevention?*

The contract should specifically state who will pay for contamination prevention measures (either directly or through a contract with a transport company). Payment schemes could take any number of forms—the buyer could pay, the farmer could pay, the farmer and buyer could split the cost by specific prevention measures, the cost could be shared in certain percentages, etc. Be sure to factor these costs into your profit estimates.

- *How will contamination prevention be accomplished?*

You may wish to spell out exactly what measures will be taken to prevent contamination and preserve organic integrity. This could be done in your contract with the buyer. Alternatively, if you are responsible for transportation and have contracted with a transportation company, it's a good idea to include these requirements in your contract with the transportation provider.

For example, the transport contract could state that your organic commodity will be transported by a bulk semi-trailer, and that the trailer and any equipment used in transport will be power-washed and air-blown. The contract could further state that the trailer will be thoroughly inspected by transport company personnel for foreign odors, residues, pests, non-organic farm products, materials prohibited under the NOP regulations, and any other substances that may compromise organic integrity. Finally, the contract could state that your commodity will not be transported with non-organic commodities or even with other farms' organic commodities—although this could increase costs if this creates a partial load.

There are many potential methods of cleaning—including dry flushing, washing, brushing, wire-brushing, sweeping, vacuuming, and sterilizing. The method required by the contract should be appropriate to both the material that needs to be removed (how it adheres) and the type of item being cleaned (whether surfaces are smooth or rough, or whether there are corners and/or crevices). Items to be cleaned could include transport vehicles (farm wagons, common carriers, tankers, trucks, etc.), shipping containers, packaging, transport equipment (augers, shovels, tarps, etc.), or storage facilities.

The contract could also detail how shipping containers and/or vehicles should be properly sealed.

- *Does the contract require “clean transport” documentation?*



Many organic contracts require “clean transport affidavits” as one technique to protect organic integrity. Clean transport affidavits are documents used to verify the maintenance of a product's organic integrity during transport and can be useful even if the contract does not require them.<sup>11</sup> A typical affidavit will generally state the farmer's name, the date the transport unit was loaded, the type of transport, who arranged the transport, the nature of the previous load hauled in the unit (especially if it was not organic), any cleaning and/or inspection measures taken, and a statement that the transport unit was inspected and cleaned thoroughly using the method indicated. The person operating the transport vehicle will be asked to sign and date an affidavit provided either by the farmer or the transport company.

Of course, a clean transport affidavit is only as trustworthy as the person who signed it. If feasible, many farmers will conduct their own inspection of transport units prior to accepting a clean transport affidavit.



- *Try to limit your obligation to prevent contamination to factors within your control.*

Contract language that states a farmer shall take “all measures” to prevent contamination potentially requires the farmer to take extremely expensive measures that are not cost-effective. You do not want to open yourself up to a claim that you did not take every possible contamination prevention measure (regardless of cost or effectiveness). Instead, you want to limit your contamination prevention responsibilities to reasonable measures and events within your control.

If you do not wish the contract to detail particular required measures for contamination prevention, you could maintain flexibility and still limit your obligation somewhat by using language stating that you will take all “reasonable” measures or “commercially reasonable” measures, or that you will use “best efforts” to prevent contamination.



Overly Broad Example: Farmer Responsibility for Preventing Contamination

Seller shall take all measures to prevent contamination of the grain with any other variety or contaminants during transport, handling, growing, harvesting, and storage of the grain.

**Who bears the risk of loss if the organic commodity is contaminated or lost in transit prior to delivery?**

Unless the contract provides otherwise, the risk of loss generally stays with the owner of the commodity at the moment it was lost or contaminated. During transit, however, it is often not obvious who owns the commodity. One way to tell if a change in ownership has occurred is if the “title” to the commodity has changed hands—often called “passage of title” or “title transfer.”

To determine who will bear the risk of loss or contamination, first look to see what the contract says about risk of loss or title transfer. The language of the contract is especially important here because title to goods can pass from the seller to the buyer in many ways and at various points along the sales chain, as determined by state law and any conditions explicitly

agreed by the parties.<sup>12</sup> If the contract is silent, consider whether you wish to rely on state law (discussed below) or negotiate clear rules on risk of loss and title transfer.

**Risky Example: Seller Retains Ownership Through Processing**

Until delivery and acceptance by Buyer at Buyer's facility, all risk of loss, damage or deterioration shall be borne by Producer, and Producer assumes all responsibility and liability incident to the planting, growing, harvesting, storage, and delivery of the crop. Transfer of title from Producer to Buyer does not occur until the crop has been entirely processed and/or cleaned.



If the contract does not explicitly address title transfer, state law likely provides “fallback” rules. Each state has its own rules, but if your state has adopted Article 2 of the Uniform Commercial Code (U.C.C.), as most have, the following rules are most likely to apply:

- If the contract requires delivery at a specific destination (but does not require or authorize you to ship by carrier), title passes from the farmer to the buyer upon physical delivery of the organic product at the specified destination.
- If the contract requires or authorizes the farmer to send the goods to the buyer, but does not require the farmer to deliver them to a specific destination, title passes to the buyer at the time of shipment.
- If the contract requires or authorizes the farmer to ship organic products by carrier, but does not require the farmer to deliver the products to a particular destination, the risk of loss passes to the buyer when the goods are delivered to the carrier. Note this only applies when there has been no breach by the organic farmer.<sup>13</sup>
- If the buyer rejects the goods (rightfully or wrongfully), even after delivery, title automatically returns back to the farmer.<sup>14</sup>

## DELIVERY

### Is “delivery” defined in the contract?

One issue related to the risk of loss discussed in the prior section can be determining the exact point in time when the product is considered “delivered” or “accepted.” Is the product “delivered” when the truck arrives at the buyer’s facility? When it is unloaded? When it is physically taken inside the facility? These seemingly minor details can take on great importance if a dispute arises, because delivery and acceptance are often crucial to the determination of whether risk of loss has passed from the farmer to the buyer. To avoid confusion on this issue, consider defining “delivery” and/or “acceptance” in the contract.



#### Example: Definition of “Delivery”

For purposes of clarity, with respect to any delivered commodity, “delivery” shall be deemed to occur upon the unloading of bins at Buyer’s facility dock.

### What are the delivery requirements?

Consider These Questions When Examining the Delivery Provisions of an Organic Contract:

- *Where is the delivery location?*

Will the organic commodity be delivered to the buyer’s facilities or somewhere else? If the shipping destination involves added costs, you may wish to negotiate a different destination or a cost-sharing plan.

- *Is there a set delivery date? Are you required to notify the buyer if delivery will be late?*
- *Is the delivery deadline tied to a shipping date or a delivery-at-location date?*

As a general rule, it is safer to tie the delivery deadline to the ship date rather than the actual delivery date. While you have some control over the date you ship out your organic farm products, you have much less control over what happens after the products have been entrusted to a delivery person or a transport company. If the buyer will not agree to a ship-date deadline, you may want to negotiate for a delivery window instead of a hard and fast delivery date.

Example: Ship-Date Deadline

All organic kidney bean deliveries must be shipped by November 15, 2012.



- *Is the delivery destination certified organic?*



Organic products will lose their organic status if they are handled by a non-certified facility. This may seem obvious, but farmers have sometimes been directed to deliver organic products to non-organic facilities. The contract should state that the delivery destination will be a certified organic facility. That way, if the farmer is directed to a non-organic operation, he/she can refuse delivery and maintain organic integrity and certification.

Farmers who are directed to deliver certified organic products to a non-certified facility should be extremely cautious. At the very least, the farmer should contact the buyer prior to delivery to discuss arranging delivery to a certified facility.

Farmers and buyers could agree in writing (either in the contract or as a contract addendum) that loss of organic certification due to delivery to a non-certified facility will not be a basis for rejection of the organic product or a reduction in the farmer's price. However, this is not a recommended practice, as loss of organic certification is permanent and would prevent product rejected on any other basis from being re-sold as organic.

- *What happens if the delivery is late?*

The contract should make clear what will happen if the shipment (for ship-date deadlines) or delivery (for delivery-date deadlines) is late. Will fees or discounts be applied? Will the shipment be rejected? Is there any leeway or grace period? Will the farmer be required to reimburse the buyer for any costs incurred as a result of the delayed shipment or delivery?

To prevent losses based on late shipment or delivery, think about the delays that could reasonably occur in your production cycle and try to build an appropriate cushion into the contract deadline. You may also wish to build in different levels of penalties for late shipment or delivery, based on the length of the delay.

In general, if you must agree to penalties for lateness, it is safer to agree to penalties in a set amount rather than open-ended penalties. For example, if you agree to reimburse the buyer for all costs it incurs as a result of the delay, you have no control over the amount that could be claimed. Instead, to limit your risk, consider negotiating flat fee penalties or penalties based on the number of days the shipment or delivery is past the deadline.

Be cautious about signing a contract that requires you to agree that any late shipment or delivery harms the buyer. In some situations, late shipment or delivery may not affect the buyer at all. Nevertheless, if you have agreed to a contract provision stating in advance that late shipment or delivery harms the buyer, the buyer could sue you for whatever amount of money she believes would compensate her for the “harm,” and you would likely be prevented from arguing that there was no harm.

- *When can products be shipped?*

The contract should make clear when the product can be shipped. Can you ship products immediately after harvest (or production, or slaughter), or must you wait until the buyer calls for delivery (that is, is delivery at the buyer’s discretion)? If delivery is at the buyer’s discretion, do you have appropriate storage options available if you are required to wait after harvest or production to deliver? What happens if the buyer calls for delivery and your commodity is not yet ready?

**Example: Buyer Calls for Delivery Times and Amounts**

Delivery Schedule: Buyer shall call for delivery at times and in amounts convenient for Buyer. Deliveries shall be, in general, completed by February 2012.



Does the buyer set out certain days and hours during which it will accept delivery? Is it possible to arrange delivery outside of normal receiving times? Will you be required to pay a fee for delivery outside the normal receiving times?

**Example: Cost to Deliver Outside Buyer's Normal Receiving Time**

Seller will deliver at agreed upon date during established receiving hours listed on Schedule C. Seller may not deliver outside of receiving hours without receiving advance Buyer permission and paying a \$100 fee.



## STORAGE (& POST-DELIVERY)

### How does the contract address storage?

Often, farmers must store their products for at least a short period of time prior to shipment. If you sell organic commodities that can be stored for an extended period of time, storage issues can become more complicated. Remember that proper storage, especially long-term storage, requires investments of time and money. Make sure to include the cost of storage in your anticipated profit calculation for any contract.

### Questions to Ask Regarding Storage

- *Does the contract make storage a likely necessity?*

As discussed above, some buyers include contract language that allows them to “call for delivery” at times and in amounts that are most convenient for them. If the delivery schedule is at the discretion of the buyer, you should make sure you have adequate and appropriate storage for your entire production (including heating or cooling as necessary) in case the buyer decides to wait a significant period of time to call for delivery. To prevent having to store commodities for an extended period of time, consider negotiating a date or time period by which the buyer must accept delivery. You may also wish to require advance payment of all or part of the contract price or a payment to cover cost of storage if the buyer fails to call for delivery by a certain date.

#### Example: Advance Payment If Buyer Is Unable to Accept Delivery

If Buyer is unable to receive shipments for any reason, Grower will provide delivery when Buyer becomes able to receive deliveries. Notwithstanding the foregoing, Buyer and Grower will agree on an advance payment if Buyer fails to accept delivery before March 15, 2013. Grower will provide adequate storage that will maintain quality of product until delivery.



- *Who pays for storage?*

Organic contracts frequently include language requiring buyers to pay farmers for storage at a certain rate (either for the entire storage period or after a certain date), or to pay a premium for stored product (such as a storage credit based on the volume of product stored).

**Example: Buyer Pays for Storage Costs**

Seller shall bear the cost of any required storage charges through the end of the calendar year; after that point, Buyer shall pay a storage credit per bushel in an amount to be mutually agreed upon by the parties.



- *Who owns the product during storage?*

It is important for the contract to make clear who owns the product during storage. Ownership could become important if the stored organic commodity suffers degradation, infestation, rot, contamination, or other damage. To protect yourself during a long storage period, you could try to negotiate contract language stating that the risk of loss of the stored product passes to the buyer after a certain date.

**After delivery (and inspection), how soon must the buyer accept or reject deliveries?**

Often, organic contracts do not address how soon a buyer must decide to accept or reject a delivery. This is likely because buyers are the primary drafters of organic contracts, and buyers may not wish to bind themselves to a set time frame. The deadline for payment can act as a stand-in for an acceptance/rejection deadline, because typically a buyer will not pay if it does not intend to accept delivery. However, if the buyer's inspection or payment timeline is long, you may wish to negotiate for an acceptance/rejection deadline that would allow you time to find another buyer in case of rejection.





### **What happens if the buyer damages or contaminates the organic products during delivery, subsequent handling, and/or processing?**

You may wish to negotiate for contract language protecting you in case of general mishandling of your product by the buyer. If the buyer rejects your delivery after causing damage or contamination during unloading, processing, or other buyer handling, it will likely be very difficult for you to find another buyer for that product. Alternatively, the buyer could contaminate or otherwise damage your shipment and still accept the delivery—but then try to penalize you for failing to meet quality standards. If possible, it is wise to use the contract to identify a point past which the buyer is liable for any damage or contamination. For example, the contract could state that liability for contamination passes to the buyer upon delivery or just prior to processing.

Shifting liability for damage to the buyer is especially important if the contract states that ownership does not pass to the buyer until after inspection or processing. Many buyers' operations are not solely organic. Thus, buyers may have non-organic products on site, or they may have recently used processing or manufacturing equipment for non-organic products. Thus, it is possible that the buyer could damage or contaminate your shipment as it awaits inspection, during transport within the buyer's facility, or during processing or cleaning.

Additionally, any delay between delivery and inspection could make it difficult to tell whether the organic commodity was damaged before or after delivery. For example, if the buyer waits until after processing to test your shipment for the presence of GMOs, it could be impossible to tell whether the shipment arrived contaminated or was contaminated during processing.

Again, even if the contract states that you own the product until after inspection or processing, you can still include contract language stating that the buyer is liable for any damage or contamination that occurs after delivery. If you are especially concerned about this issue, you could combine this language with testing or inspection upon delivery. For instance, the buyer could agree to test or inspect immediately upon receipt—or you could contract with your transportation company to perform testing or inspection upon delivery and document the results. This kind of arrangement could provide evidence that damage was, in fact, caused by the buyer—not during transport or on the farm.

Of course, perishable products—including produce, milk, and eggs—must be sampled and tested almost immediately. Storage commodities, like grain and dry beans, can theoretically be tested at any time (but preferably at least prior to processing). Regardless, the risks of

contamination and commingling increase with time and multiply each time an organic product is handled.



### **What happens if the organic farm product contaminates the buyer's other organic commodities?**

Buyers generally purchase organic commodities from multiple farms, and may (intentionally or unintentionally) mix the different farms' products together at the buyer's facility. Thus, if your delivered products are infested or contaminated, it is possible that your products could damage other organic products the buyer has purchased.

For example, if the buyer is reselling organic commodities internationally, it is possible that GMO-contaminated corn could push the GMO levels beyond the low thresholds for GMO content in places like the EU and Japan. Insect infestations could also damage the buyer's other commodities.

#### **Example: Seller Must Reimburse Buyer for Contamination of Other Commodities**

Rights: Seller shall fully reimburse Buyer for any damages related to contamination caused by Producer's organic commodity.



Given that it is difficult to ensure with 100 percent certainty that your products will not contaminate the buyer's other organic products, you may wish to negotiate contract language stating what will happen in case of cross-contamination. You could agree to reimburse the buyer's full damages related to the contamination, but this cost could be unpredictably large. Alternatively, you could agree to reimburse the buyer's damages up to a certain dollar amount. You could also negotiate contract language stating that you have no liability for contamination after your product has been accepted and inspected by the buyer.

**CHAPTER 7 — ENDNOTES**

- <sup>1</sup> U.S. Department of Agriculture National Organic Program, *Draft Guidance: Handling Bulk, Unpackaged Organic Products*, NOP 5031 (2011), available at <http://www.ams.usda.gov/AMSV1.0/getfile?dDocName=STELPRDC5096871>.
- <sup>2</sup> See 7 C.F.R § 205.307(b) (2012). See also Iowa Department of Agriculture & Land Stewardship, *Iowa Organic Certification Program: Developing a Producer Lot Number*, available at <http://www.iowaagriculture.gov/AgDiversification/Organic/LotNumbering.doc>.
- <sup>3</sup> 7 C.F.R § 205.307(a) (2012).
- <sup>4</sup> 7 C.F.R § 205.307(b) (2012).
- <sup>5</sup> See 7 C.F.R § 205.307 (2012).
- <sup>6</sup> See also U.S. Department of Agriculture Food Safety and Inspection Service, *A Guide to Federal Food Labeling Requirements for Meat and Poultry Products* (August 2007), available at [http://www.fsis.usda.gov/PDF/Labeling\\_Requirements\\_Guide.pdf](http://www.fsis.usda.gov/PDF/Labeling_Requirements_Guide.pdf) (meat and poultry labeling); see also National Agricultural Law Center, *Legal and Business Guide for Specialty Crop Producers*, at Chapter 8 (February 2011), available at [http://www.nationalaglawcenter.org/assets/articles/center\\_specialty.pdf](http://www.nationalaglawcenter.org/assets/articles/center_specialty.pdf) (specialty crop labeling); see also U.S. Department of Agriculture Agricultural Marketing Service, *Labeling Packaged Products Under the National Organic Standards* (July 27, 2009), available at <http://www.ams.usda.gov/AMSV1.0/getfile?dDocName=STELPRDC5078591&acct=nopgeninfo> (organic labeling).
- <sup>7</sup> See 7 C.F.R. § 205.272 (2012).
- <sup>8</sup> See U.S. Department of Agriculture Agricultural Marketing Service, *Instructions for Completion of an Export Certificate (TM-11)*, available at <http://www.ams.usda.gov/AMSV1.0/getfile?dDocName=STELDEV3017717>.
- <sup>9</sup> See U.S. Department of Agriculture National Organic Program, Miles V. McEvoy, Deputy Administrator, Policy Memo 10-3 at 2 (November 4, 2010).
- <sup>10</sup> For more information about EU documentation and the EU-U.S. equivalency agreement, see U.S. Department of Agriculture National Organic Program, *Accessing the European Union Organic Market* (May 25, 2012), available at <http://www.ams.usda.gov/AMSV1.0/getfile?dDocName=STELPRDC5097062> and *U.S.-European Union Organic Equivalence Arrangement Questions and Answers*, available at <http://www.ams.usda.gov/AMSV1.0/getfile?dDocName=STELPRDC5097061>.
- <sup>11</sup> For a sample clean transport affidavit, see National Sustainable Agriculture Information Service (ATTRA), *Forms, Documents and Sample Letters for Organic Producers* (2005), available at <https://attra.ncat.org/attra-pub/viewhtml.php?id=170ATTRA>.
- <sup>12</sup> See U.C.C. § 2-401(1) (1977).
- <sup>13</sup> See U.C.C. § 2-509 (1977).

<sup>14</sup> See U.C.C. § 2-401(2), (4) (1977); see also, U.C.C. § 2-509 (1977) (risk of loss rules on delivery by carrier or by bailee); see also U.C.C. § 2-510 (1977); see also, generally, U.C.C. Art. 2, Part 5 (1977) (Performance).

# 8

# Interaction With NOP Regulations

- [8-1](#) How does the contract address organic certification and enforcement?
- [8-2](#) Beware of broad termination rights related to organic principles
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## CHAPTER QUICK TIP

### **Don't Jeopardize Your Organic Certification**

Watch out for contract requirements that could cause you to violate organic regulations and potentially jeopardize your organic certification. To help prevent any buyer pressure to break NOP regulations (such as organic seed sourcing regulations), you could insert language in your contract stating that both parties agree to comply with NOP regulations in all respects.





## **ORGANIC CERTIFICATION STATUS**

### **How does the contract address organic certification and enforcement?**

#### Evidence of Organic Certification

Nearly every organic contract requires the farmer to provide evidence that the farm operation has obtained federal organic certification under National Organic Program (NOP) regulations. The contract might state that the farmer must provide the buyer with proof of certification by a particular time, such as prior to beginning production, prior to harvest, or prior to making delivery of the organic commodity under contract. The contract might even state that the buyer is not required to pay for the commodity until the buyer receives proof of organic certification.

#### Organic Certifier Requirements

Furthermore, the contract might include requirements relating to the farm's Accredited Certifying Agent (ACA or organic certifier). For example, the buyer might require the farmer to use a specific organic certifier. If you have a good relationship with an organic certifier who is not specified in the contract, you may wish to negotiate the ability to use your current certifier. However, buyers may have a valid reason to require a specific certifier, such as the need for a certifier authorized to issue international organic certifications.

#### Status of Organic Certification

The contract might also address changes in the farm's organic certification status. For example, a contract might require the farmer to notify the buyer of any change in the farm's status. If your contract has such a requirement, be sure you understand all of the types of actions the buyer would consider to be a change in status that you would be expected to report. For example, must you report complaints, investigations, noncompliance notices, proposed suspensions or revocations, mediations, or appeals? Or would you only need to report an actual suspension or revocation?

Example: Buyer Termination Due to Investigation Provision

Buyer may cancel the Agreement if any part of Seller's organic operation is under investigation for non-compliance.



It is preferable to avoid contract provisions allowing the buyer to terminate the contract if NOP merely investigates your farm for noncompliance. Farmers cannot control whether they become subject to certifier or NOP investigation; a mistaken impression or false report could potentially trigger an investigation. Even after receiving a notice of proposed suspension or appeal, farmers have the right to request mediation and/or appeal.<sup>1</sup> Under current law, participating in both the mediation process and the appeals process stops the proposed suspension or revocation from becoming final until those processes are completed.<sup>2</sup> Thus, a noncompliance investigation—or even a proposed suspension—could end up being resolved between an organic farmer, certifier, and the NOP without changing the organic status of the product under contract.

Additionally, an investigation of part of your farm might not even affect the organic product under contract if the investigation relates to a different product entirely, or a portion of your production that is not needed to fulfill the contract.

**Beware of broad termination rights related to organic principles.**

Watch out for contract language giving the buyer broad rights to terminate the contract if you “act inconsistently with organic production principles” or something similar. “Organic production principles” appear to be broader than the actual NOP regulations, and such a provision would therefore potentially allow the buyer to terminate the contract even if you were in full compliance with the NOP regulations.





**Example: Buyer Termination Due to Noncompliance with Organic Principles Provision**

Buyer may cancel the Agreement if Seller is involved in any activity inconsistent with the principles underlying organic production, or if such activity is the subject of publicity (including via electronic media).

The language in the example above is much broader than necessary to protect an organic buyer's interest. A narrower provision, perhaps allowing termination upon suspension or revocation of certification, would protect the buyer while not allowing unjustified or premature termination. Language requiring the farmer to provide notification of a noncompliance investigation would not be unreasonable, provided that the buyer cannot terminate the agreement if the farmer provides adequate assurance that the organic contract will be fulfilled.<sup>3</sup>



**Example: Buyer Rights Upon Investigation or Revocation/Suspension of Organic Certification**

Buyer may terminate the contract if the organic crop under contract is subject to suspension or revocation of organic certification. Producer agrees to notify Buyer of any investigation or notice of noncompliance with NOP regulations; however, Buyer may not terminate the contract solely due to investigation or notice of proposed suspension/revocation if Producer provides adequate assurance that Producer will be able to fulfill the contract by providing a certified organic crop meeting contract specifications.



## PROHIBITED SUBSTANCES AND GMOS

### **How does the contract address pesticide residues and other prohibited substances?**

#### NOP Regulations on Prohibited Substances

Although the NOP regulations state that farm products cannot be sold as organic if residues of pesticides or prohibited substances exceed five percent of U.S. Environmental Protection Agency (EPA) tolerances, the NOP regulations do not mandate regular testing for these substances.<sup>4</sup> Instead, organic certifiers may test if there is reason to believe that an organic product or input has come into contact with a prohibited substance or has been produced using excluded methods (such as genetically modified organisms (GMOs)).<sup>5</sup>

Prohibited substances are typically synthetic substances, although some natural substances are also prohibited.<sup>6</sup> (GMOs are also prohibited, as discussed in the next section, but the NOP regulations refer to GMOs as “excluded methods” rather than “prohibited substances.”)<sup>7</sup> The “National List” is the portion of the NOP regulations that lists particular allowed and prohibited materials.<sup>8</sup> All synthetic materials are prohibited for organic crop and livestock production unless they are specifically approved by NOP and appear on the National List. All natural products are allowed, unless they are specifically prohibited and appear on the National List.

#### Testing Requirements Beyond NOP Regulations

If the contract requires that your organic commodity be tested for pesticides or other prohibited substances, know that this is a requirement that goes beyond the NOP requirements. If your contract requires testing, keep these considerations in mind (as discussed in more detail in Chapter 6, pages 6–20 through 6–24):

- Who will pay for the initial testing? (Ideally, the buyer.)
- Who will conduct the test? Will it be a specially qualified individual? Is there a testing protocol? (Ideally, a qualified individual with a testing protocol.)
- When will the test be conducted? Prior to shipment, upon delivery, or after processing? (Ideally, prior to shipping or immediately upon delivery.)
- Where will the test be conducted? In the field, at the buyer's facility, in a sterile environment, or in a laboratory? (Ideally, in a sterile environment or in a lab.)
- What are the test criteria? What is the test measuring? What is the rejection level? (Ideally, the contract should state a specific rejection level for any testing.)
- Can you dispute a test result you disagree with and, if so, how? Can you get an independent test, and/or a laboratory test? Who will pay for any additional testing? (Ideally, the contract should include a dispute resolution mechanism that includes independent testing paid for at least in part by the buyer.)
- Will you have access to the test samples? (Ideally, yes.)

### Keep Your Own Samples

Consider keeping duplicates of any samples you send to the buyer, and, in addition, including language in the contract allowing you access to any samples tested by the buyer.

### Beware of Contract Prohibitions on “All Synthetics”

Some organic contracts will prohibit all synthetic herbicides, vaccines, antibiotics, hormones, and other substances. Keep in mind that the NOP regulations allow some synthetics in organic production (those that appear on the National List). If your contract has a blanket prohibition on synthetics or chemicals, you should double-check your inputs to make sure they are both approved for organic production and are also non-synthetic. If you cannot easily do without a particular NOP-approved synthetic, consider negotiating a specific exception for that substance.

### **How does the contract handle GMOs?**

Genetically modified organisms (GMOs) pose a serious threat to farmers who grow organic crops for which there is a GMO equivalent. Although

there are many steps farmers can take to reduce their risk of GMO contamination, it is almost impossible to guarantee that a crop is 100 percent GMO-free. This is especially true for farmers who grow organic corn or organic soybeans, because the GMO varieties of these crops are so prevalent. Currently, the U.S. Department of Agriculture (USDA) has approved over 15 types of GMO crops that may be planted without governmental oversight. These include corn, sweet corn, soybeans, canola, cotton, flax, alfalfa, sugar beets, tobacco, potatoes, squash, papaya, linseed, rice, plums, and tomatoes.<sup>9</sup> GMO wheat is not approved for planting as of the date this guide was written, but it has been approved for trial plots.

#### NOP Regulations on GMOs (Mere Presence Not Prohibited)

Federal organic regulations do not require that certified organic farm products be entirely free of GMOs. The regulations simply prohibit the use of GMOs in organic production.<sup>10</sup> Organic farmers are required to create appropriate buffer zones and adopt appropriate handling practices to protect the crop from contamination.<sup>11</sup> Nonetheless, if drift from a neighboring farm introduces GMOs to your organic crop, your crop can still be certified organic—as long as you fulfilled all of the other organic requirements. Similarly, if a truckload of certified organic soybeans produced in compliance with the organic rules tests positive for the presence of GMOs, the status of the soybeans' organic certification remains unchanged.

Although a farm's organic certification is not at risk due to the mere presence of GMOs if organic practices have been followed, buyers may still expect 100 percent non-GMO compliance and reject your organic production if the certified organic commodity tests positive for any level of GMOs. Consequently, you may wish to consider the issues discussed below prior to signing an organic contract.

#### Does the Contract Address GMOs?

Farmers should know what their buyers' expectations are regarding the presence of GMOs in the organic product under contract. Accordingly, if your contract is silent on GMOs, make sure to ask about buyer expectations, and consider working with the buyer to fully describe the buyer's GMO-related expectations in the contract text.

An easy way to address GMOs without agreeing to specific anti-contamination measures or testing protocols is to simply state that you will comply with the NOP regulations regarding GMOs. This language should reassure the buyer that you will not use GMO seed, that you will not feed GMO crops to organically managed animals, and that you will

take appropriate measures to prevent GMO contamination as detailed in your Organic System Plan.



Good Example: Compliance with NOP Regulations on GMOs Provision

Seller and Buyer agree that all measures taken by Seller related to genetically modified organisms (GMOs) will comply with the federal organic regulations regarding organic production (the NOP regulations).

Does the Contract Set a GMO Rejection Level?

If you discover your buyer does have expectations about the presence of GMOs or GMO levels, your organic contract should state the GMO rejection level or range. The “rejection level” is the percentage of GMOs present in your organic commodity that will trigger rejection of your shipment. This is critical information, because if the contract prohibits GMOs but does not state a rejection level, the buyer could reject your shipment if it has even a tiny presence of GMOs.

GMO-Free Standards

With the rise of GMOs in the United States since the late 1990s, it is increasingly difficult for organic farmers to maintain 100 percent GMO-free products,<sup>12</sup> especially after an organic commodity has been exposed to potential GMO contamination during transportation and delivery. Due to this difficulty, farmers should be cautious about representing that their contracted organic commodities are 100 percent GMO-free.

There is no legal standard for the meaning of “GMO-free” in the United States. “Certified organic” status is the only legal standard that prohibits the use of GMOs in the production process. However, the U.S. market’s rejection level for “GMO-free” commodities is often considered to be .9 percent, based on the level for mandatory GMO labeling in the European Union.

Some buyers, having experienced difficulty obtaining 100 percent GMO-free farm products, will agree to pay a premium for organic commodities that are entirely free from the presence of GMOs. Consider negotiating a GMO-free premium structure with your buyer if you are absolutely

confident that you can provide GMO-free crops or livestock—or if you are willing to risk rejection based on the unintended presence of GMOs.

### Does the Contract Require Measures to Prevent GMO Contamination?

If your contract calls for measures to prevent GMO contamination in addition to those set forth in your Organic System Plan, make sure the anti-contamination measures are feasible and that you can afford the time and money required to carry out those measures. Please see pages 8–11 through 8–13 of this chapter for a discussion of anti-contamination measures and corresponding contract considerations in the transportation context.

### Does the Contract Require GMO Testing?

Some organic buyers require that organic farm products be tested for the presence of GMOs.

- *Types of GMO Tests*

The first consideration to discuss with the buyer is what type of GMO test will be conducted. There are two major types of GMO tests.<sup>13</sup> The first is known as a “strip test” that can be used in a field setting to immediately detect the presence of modified DNA. Strip tests allow rapid, on-site results, but can produce false positives and cannot detect the precise percentage of GMOs in a sample. Additionally, multiple strip tests could be required for the same commodity, because each test can only detect one out of the many types of genetic modifications that exist.

The second type of GMO test, the PCR (polymerase chain reaction) test, is much more precise than a strip test but must be conducted in a laboratory at a higher cost. The PCR test method is recognized as more sensitive and reliable than any other GMO test method, and it can determine the precise percentage of GMOs in a sample. Moreover, when proper protocols and samples are used, it is extremely rare for a PCR test to produce a false positive or false negative result. Thus, if accuracy is extremely important, the PCR test should be used instead of the strip test.

- *Questions to Ask About GMO Testing*

You should discuss the following questions related to GMO testing with your buyer and consider including the details of the discussion in your contract:

- Who will pay for the initial test (or tests)? (Ideally, the buyer.)
- Who will conduct the test? Will it be a specially qualified individual? Is there a testing protocol? (Ideally, a qualified individual with a testing protocol.)
- When will the test be conducted? Prior to shipment, upon delivery, or after processing? (Ideally, prior to shipment or immediately upon delivery.)
- Where will the test be conducted? In the field, at the buyer's facility, in a sterile environment, or in a laboratory? (Ideally, in a sterile environment or in a lab.)
- What are the test criteria? What will the test measure? What is the rejection level? (Ideally, the contract should state a specific rejection level for any testing.)
- Can you dispute a test result you disagree with and, if so, how? Can you get an independent test, and/or a laboratory test? Who will pay for any additional testing? (Ideally, the contract should include a dispute resolution mechanism that includes independent testing paid for at least in part by the buyer.)
- Will you have access to the test samples? (Ideally, yes.)

You might also consider negotiating contract language calling for initial DNA strip tests, with PCR as a backup for any shipments that test positive for GMOs.

Example: GMO Testing Provision

Organic product must test negative for GMOs. Product will be tested via "strip test" mechanism upon delivery. Shipments that test positive for the presence of GMOs will be re-tested once. Buyer shall bear the cost of these tests. Producer will be notified within one business day of any positive GMO tests. Producer may opt for a PCR test at Producer's expense; PCR results will be final.



### Does the Contract Require GMO-Free Documentation?

Instead of testing for GMOs, some organic contracts may require documentation of farmers' GMO-free production processes. For example, farmers could obtain verification from their seeds and planting stock suppliers affirming that each variety of seed and planting stock is not the product of genetic engineering or GMOs and has not been treated with synthetic materials prohibited by the NOP regulations. These verifications are generally signed by an authorized representative of the company selling the seed or planting stock.

### GMO-Free Labeling and Certification

As consumers become more aware of GMO-related issues, some organic handlers are beginning to use "GMO-free" labeling as a marketing strategy. No state or federal government has enacted a GMO labeling law (although labeling bills have been introduced in Congress and in state legislatures nationwide) or even created a certification system for GMO-free products. Thus, while some organic food companies simply use a version of the words "GMO-free" on their packaging, some organizations have created private non-GMO certification programs to fill the labeling gap. Companies using either approach are likely to be even more interested in ensuring that farmers supply them with documentation that products supplied are GMO-free.

#### **The Non-GMO Project**

The Non-GMO Project is a non-profit organization that has developed a process-based standard for verification of non-GMO status. Companies that achieve certification of their non-GMO status are allowed to use the Non-GMO Project label as a marketing tool. The Non-GMO Project verification system and certification is increasingly being required by larger organic buyers. For more information about the Non-GMO Project, see [www.nongmoproject.org](http://www.nongmoproject.org).



If your contract requires you to obtain a non-GMO certification in addition to organic certification, be sure to factor the time and cost of this additional certification into your calculation of what you are likely to earn under the contract. If the additional certification seems likely to be too



burdensome, consider negotiating for GMO testing or GMO-free documentation as substitutes for the certification.

### Protect Yourself From GMOs

In addition to carefully considering the questions above, you can take steps to help protect yourself from GMO contamination and, thus, from GMO-related contract problems. As mentioned above, it is a good idea to obtain non-GMO affidavits from seed and other input suppliers when applicable. Furthermore, you should retain receipts documenting your inputs, seed tags, letters from seed suppliers, and copies of any GMO test results. You can also take photographs to document the existence of buffer zones, runoff diversions, windbreaks, and other anti-contamination efforts.<sup>14</sup>

### **Does the contract have specific isolation, buffer, or other anti-contamination requirements?**

#### NOP Regulations on Anti-Contamination Measures

NOP regulations require “necessary” measures to prevent contamination by pesticides, GMOs, and other prohibited substances, but do not require farms to take specific actions.<sup>15</sup> Organic farmers must, however, work with their organic certifiers to include specific anti-contamination measures in their Organic System Plans (OSPs) that are appropriate to their particular farm operations. Farmers must comply with their OSPs once the OSPs have been approved. Generally, the anti-contamination measures include buffer crop plantings, windbreaks, no-spray signs, and neighbor notification.

Under the NOP regulations, any equipment used for both organic and non-organic (conventional, transitional, and buffer) production must be thoroughly cleaned prior to each use in an organic crop.<sup>16</sup> This includes planting equipment, haying equipment, tarps, harvesting equipment, grain handling/drying equipment, on-farm wagons, trailers, trucks, storage units, etc.

Note that your contract may require particular anti-contamination requirements that go beyond what is in your OSP. Does the contract require particular signage (such as “NO SPRAY” signs of a particular size or color), neighbor notification within a certain distance, equipment clean-out logs, or specific sizes or locations of buffer crop plantings?<sup>17</sup> If your contract requires specific anti-contamination measures, make sure those measures are both (1) feasible, and (2) consistent with your OSP. If you have concerns about how the contract requirements will fit with

your OSP, communicate with your organic certifier before signing the contract.

### Other Contract Concerns Related to Anti-Contamination Measures

- *Avoid promising too much.*

One contract pitfall to avoid is a provision stating you will “prevent all risk of contamination and protect organic integrity” or similar language. No matter how many preventative measures you take, you cannot prevent all risk of contamination, so it is best not to promise that you can. Similarly, try to avoid promising that you will make “all efforts” or take “all measures” to prevent contamination. That kind of language implies you will take every possible measure (regardless of cost or effectiveness) to protect your crop, and if you don’t, you could be in violation of the contract.

Instead, consider negotiating language stating you will take “reasonable measures” or “commercially reasonable measures.” That way, you are limiting your promise to a smaller range of anti-contamination measures. Or, you could specify exactly what you are required to do (specify the size of buffer zones, specific handling practices, etc.). That way, both you and the buyer are on the same page as far as what steps you are contractually required to take to prevent unwanted drift or other contamination. Or, you could simply state that all measures taken to prevent commingling and contamination will comply with NOP regulations.

#### Good Example: Anti-Contamination Provision

In order to prevent contamination of the organic product subject to this Agreement, Grower agrees to take commercially reasonable anti-contamination measures in compliance with NOP regulations.



- *Who pays for anti-contamination prevention?*

In most cases, the farmer will be expected to pay for all anti-contamination measures because contamination prevention—for better or worse—has become an integral part of organic farming. In a best-case scenario, contamination prevention costs should be

offset somewhat by the organic premium. However, if the buyer wants to require specific anti-contamination measures that are outside the normal bounds for organic operations, consider negotiating a cost-sharing structure (or simply an increased base price) to compensate for those measures.



## **ACCESS TO PASTURE AND THE OUTDOORS**

### **Does the livestock or poultry contract address access to pasture or access to the outdoors?**

#### NOP Regulations on Access to Pasture

If the livestock or poultry contract requires “access to pasture,” is it clear what that term means? Under the NOP pasture standard for livestock, 30 percent of organic livestock’s dry matter intake must be grazed from organically managed pasture throughout the entire grazing season, which must total at least 120 days per year.<sup>18</sup>

#### Recommendations on Access to Pasture

If your contract references access to pasture, you may wish to consider the following:

- Is the contract definition of “access to pasture” the same as NOP’s definition, or is it more or less stringent?
- If the contract requires more access to pasture than the NOP regulations require, be sure that grazing more than 30 percent of dry matter intake is feasible with respect to: (1) the amount of organic pasture you can grow or rent; (2) the number of animals you raise; and (3) your local climate.
- Does the contract include exceptions to the pasture requirement for severe weather, such as drought or flooding? If not, consider building in disaster and weather-related exceptions. The NOP regulations provide exceptions in such cases through “temporary variances,” discussed in more detail in Chapter 4, page 4–6. You may wish to ensure that your contract either: (1) defines “access to pasture” as “compliance with NOP access-to-pasture rules”—which will build in the temporary variance safety valve; or (2) expressly excuses you from access-to-pasture obligations for livestock in case of severe weather or disaster.



Good Example: Access to Pasture Provision

Seller will provide access to pasture in accordance with the NOP regulations on pasture, including the regulations providing NOP-declared temporary variances from NOP regulations.

NOP Regulations on Access to the Outdoors

Similarly, if your contract requires “access to the outdoors” for poultry or other livestock, is the contract clear about what that term means? With certain exceptions, the NOP regulations require year-round access for all animals to the outdoors, shade, shelter, exercise areas, fresh air, clean water for drinking, and direct sunlight of a type suitable to the species, its stage of life, the climate, and the environment.<sup>19</sup> The current outdoor access requirements (listed in the NOP regulations under “Livestock Living Conditions”) are rather vague, and the National Organic Standards Board (NOSB) and NOP are currently studying how to clarify “access to the outdoors” in preparation for potential future rulemaking.<sup>20</sup>

Recommendations on Access to the Outdoors

If your contract references access to the outdoors, you may wish to consider taking the following steps:

- Either define “access to the outdoors” requirements as “in accordance with NOP regulations,” or state specific requirements in the contract (for example, five outdoor square feet per laying hen).
- If your contract does include specific outdoor space requirements, consider whether you can physically provide that amount of space.
- Be certain you can afford to provide the required outdoor access.
- If the contract requirements that exceed NOP regulations seem too burdensome, consider negotiating language that allows you to maintain your current practices or make an affordable upgrade.



## ORGANIC SEED ISSUES

### How does the contract handle organic seed requirements?

It is important for organic farmers and buyers to be in agreement about the use of certified organic seed for growing certified organic crops.

#### NOP Seed Regulations

The NOP regulations on seed require farmers to use certified organic seed (and certified organic transplants)—unless the farmer can document that organic seed (or transplants) are not commercially available.<sup>21</sup> “Not commercially available” means unavailable from organic sources in the form, quality, quantity, or equivalent variety necessary for the organic operation. If the organic seeds you need are not available, you must provide proof to your certifier that you made good-faith efforts to obtain organic seed.<sup>22</sup> Keep in mind that high price is not an excuse for failing to purchase organic seed.

If certified organic seed is not commercially available, the NOP regulations allow farmers to use untreated, non-GMO, conventionally grown seed.<sup>23</sup>

#### Contract Issues Regarding Organic Seed

Although the NOP seed regulations may seem relatively straightforward, problems can arise when organic contracts attempt to impose requirements that are either stricter or more lenient than the regulations. For example, a buyer may want to require a farmer to use a particular type of seed even though it is not certified organic. On the other hand, an organic contract might require organic seed with no exception for cases when certified organic seed is not commercially available. A farmer who diligently satisfies all of the NOP regulations could still run into trouble with a buyer who is expecting certified organic seed to be used (even if the contract doesn't explicitly say so), and later finds that the farmer used conventional seed.

While the farmer's use of conventional seed might have been in perfect compliance with the NOP regulations due to commercial unavailability,

the buyer might reject the delivery based on its assumptions about the use of organic seed.



**Example: General Agreement to Comply With NOP Regulations on Seed**

Grower and Buyer agree that Grower will comply with the federal organic regulations (NOP regulations) regarding organic seed sourcing.

Because of these risks for confusion and conflicting expectations, consider the questions discussed below when reviewing an organic contract for crops to be grown from seed, seedlings, or transplants.

**Does the contract address seed?**

If the contract makes no mention of seed, make sure the buyer understands that you will plant certified organic seed for the contracted organic crop if it is commercially available. Make sure the buyer understands that if certified organic seed is not commercially available, you will plant untreated, non-GMO conventional seed. You may wish to include this language in the contract, or language similar to the following: “Seller and Buyer agree that Seller will comply with the federal organic regulations regarding organic seed sourcing.”

**Obtain Documentation and Keep Records**

If you are unable to find certified organic seed, make sure to keep records of the efforts you made to find organic seed, including names and contact information of seed and planting stock suppliers, and notes about quantity, quality, and form. You will need this documentation for your organic certifier, and the buyer may wish to see it as well. Additionally, if you purchase non-organic seed, it is wise to obtain written verification from the seed supplier that the seeds are untreated and non-GMO, especially if the type of seed you purchase has a GMO equivalent.<sup>24</sup>

### **Does the contract require you to plant a particular type of seed?**

If the contract requires you to plant a particular seed variety, check to see whether the seed required by the contract is certified organic. If it is not organic, check to see whether a certified organic version of the seed is commercially available before signing the contract. If there is a certified organic version available, the NOP regulations require you to use the certified organic variety. In order to avoid violating the NOP regulations, you may wish to negotiate with the buyer to ensure the contract allows for the use of the certified organic seed variety.

### **Does the contract require you to plant seed provided by the buyer?**

If the contract requires you to plant buyer-provided seed, you may wish to address the following factors in your contract:

#### Quality

You may wish to negotiate contract language requiring the buyer to provide seed of good quality. You might wish to further require the buyer to: (1) reimburse you for all losses you may incur as a result of bad quality seed (including lost profits), and (2) protect you from any consequences resulting from bad quality seed. It would not be fair, for example, for you to bear the cost of replanting poor quality seed. Even worse, it would be unfair for you to lose an entire crop as a result of poor quality seed. Additionally, if the resulting crop fails to meet the contract quality standard as a result of bad seed, it would be unfair for the buyer to penalize you for poor quality upon delivery. Thus, you may wish to include language stating that, if the resulting crop does not meet the buyer's contract quality standards due to low-quality buyer-provided seed, the buyer will purchase the crop at the contract price that would have been paid for contract-quality seed.

Moreover, consider including contract language preserving your right to: (1) reject any seed that is of poor quality; (2) request substitute seed; and/or (3) procure substitute seed from another supplier. You may also wish to require the buyer to provide test results and/or affidavits that show the seed is uncontaminated and of the appropriate quality.

#### Proof of Commercial Unavailability for Non-Organic Seeds

If the buyer provides you with non-organic seed, the buyer should also provide proof that organic seed is not commercially available for that variety. This proof should be the same kind of evidence that organic



farmers provide to certifiers showing that the buyer conducted a good faith search for organic seed (as discussed on page 8–17 of this chapter).

You may also wish to have an affidavit from the buyer's supplier certifying that the non-organic seed is both untreated and non-GMO.

### Agricultural Production Methods

The buyer may wish to require particular agricultural production methods in conjunction with buyer-supplied seed. You may wish to clarify whether you are bound to follow the agricultural production methods or whether they are simply advisory. Additionally, if you follow required production methods and, as a result, the crop is unsuccessful, does the contract protect you from losses resulting from the contract's required production methods?

### Timeliness of Seed Delivery

Does the contract require the buyer to deliver the seeds in a timely fashion? You may wish to negotiate contract language obliging the buyer to deliver the seeds by a certain date to ensure timely planting. Also, you may wish to include a penalty for the buyer's late delivery, such as a set financial penalty or a promise to reimburse you for any losses caused by late delivery.

### Payment

Will the buyer be providing the seed free of charge, or will you be required to pay for it? If you are required to pay for it, can you purchase it from any supplier, or do you have to purchase it from the buyer? If you have to purchase it from the buyer, is the buyer's price competitive with other suppliers?

Additionally, who is required to pay for shipping? If you will be covering the costs, can you choose the freight company, or will you have to reimburse a company of the buyer's choosing?

### Bonus for Planting Particular Seed

Does the contract provide any type of bonus if you agree to plant a particular seed? For example, a buyer might agree that a farmer who plants a seed with particular properties (such as a high protein content) will automatically qualify for a premium payment rate.

### Adapted to Local Conditions?

You may also wish to ensure that the contract requires buyer-provided seed to be adapted to local conditions—including your soils and climate.

**Don't Jeopardize Your Organic Certification**

If you plant conventional seed in violation of the NOP regulations, you jeopardize your organic certification status. Keeping the severity of this consequence in mind, you may wish to negotiate language in the contract to require a buyer who supplies seed to provide either: (1) certified organic seed; or (2) proof of the commercial unavailability of organic seed that you provide to your certifier.

**Example: Buyer Provides Proof of Commercial Unavailability Provision**

If Buyer provides Seller with non-organic seed, Buyer agrees to provide Seller with written documentation showing that Buyer has complied with the NOP regulations on organic seed (i.e., that organic seed is not commercially available within the meaning of the NOP regulations, and Buyer has attempted to source organic seed from a number of providers). Furthermore, if organic seed is not commercially available, Buyer agrees to provide Seller with written documentation showing that the seed provided is untreated, non-GMO, and free of contamination.

**Does the contract place restrictions on your use of buyer-provided seed or the resulting crop?**

Some organic contracts include strict rules about how farmers must handle buyer-provided seed. These restrictions can have serious consequences, as discussed below.

Questions to Consider Regarding Buyer-Provided Seed Restrictions:

- *Do you have to account for how buyer-provided seed was used?*

If you have to account for how you used the seed, you may wish to ensure the contract states how this accounting should be accomplished.

- *Do you have to promise not to give the seed to anyone else?*

If you make a contract promise that you will not give the seed to anyone else, be careful to comply with this provision. The buyer could sue you for considerable damages if your failure to keep the seed to yourself results in a competitor gaining access to proprietary seed.

- *Do you have to return any unused seed?*

If you must agree to return any unused seed to the buyer, the contract should state who must pay for the return of the unused seed.

- *Can you sell crops grown from buyer-provided seed to another purchaser?*

If you are permitted to sell crops grown from buyer-provided seed only to the buyer, you should seriously consider negotiating a safety valve provision for rejected or unpurchased product. Without such a provision, you could end up in a situation where even though the buyer refuses to pay for or rejects your crop, you are prohibited from finding another willing buyer. In that situation, you could lose the benefit of an entire season's harvest.

**Example: Buyer Maintains Control of All Seedstock Provision**

Seller shall use the proprietary seedstock provided by Buyer and shall account for and return any unused seedstock. Any production from the seedstock shall be delivered to Buyer, or otherwise accounted for. In no case shall crops produced by Seller for Buyer be given or sold to any other purchaser. Seller shall not retain seedstock, or save seeds from the resulting crop.

**Allowing for an exception through written permission:**

Producer agrees that no soybeans will be saved, sold to any other parties, or used for seed purposes without written permission from Buyer.



To prevent losses related to rejection of crops resulting from restricted buyer-provided seed, you should seriously consider including contract language that allows you to find another purchaser for any portion of the crop that the buyer refuses to purchase or rejects for any reason (including any amounts in excess of the estimated harvest).



**Example: Allowing Farmer to Sell Crop Elsewhere  
If Buyer Rejects or Fails to Pay**

In return for Buyer's agreement to purchase all crops grown from seed provided by Buyer at the full contract price, Seller agrees that crops produced by Seller for Buyer shall not be given or sold to any other purchaser. Seller further agrees that Seller shall not retain seedstock, or save seeds from the resulting crop. However, should Buyer reject Seller's delivery, fail to pay Seller fully or promptly, or otherwise fail to purchase all crops grown from seed provided by Buyer at the full contract price, Buyer agrees that Seller may cover by selling crops grown from seed provided by Buyer to another purchaser.



## **ACCESS TO RECORDS, SPLIT OPERATIONS & TRANSITIONAL SUPPORT**

### **Does the contract give the buyer access to your organic records (or to your certifier's records)?**

Some organic contracts require farmers to allow buyers access to farm records. The main concerns with such provisions are issues of timing and scope.

#### Timing of Buyer Access to Records

Does the contract allow the buyer access to your records “at any time?” If so, you could potentially be in violation of your contract if you refuse your buyer access even at inconvenient times like midnight on Christmas Eve. Therefore, it’s better to include language limiting the buyer’s access to “reasonable times” or “during business hours.”

#### Scope of Buyer Access to Records

Similarly, you may wish to limit the buyer’s access to only certain kinds of records, or only records from a certain time period. If your contract allows access to “all records,” the buyer may rightfully have access to all of your records—not just organic or farm records. Furthermore, such open-ended language could allow the buyer access to records going back decades. Therefore, consider whether the buyer’s access to your records should be limited in time (for example, the last five or ten years) and in type (for example, organic records for this farm).

#### Direct Access to Certifier Records and NOP Certifier Disclosure Rules

Some organic contracts require that the buyer have direct access to records held by the farmer’s organic certifiers. Sometimes, buyers require farmers to sign “releases” allowing the certifier to directly send records or information to the buyer.

The NOP regulations require certifiers to keep non-public farmer information confidential unless the farmer has given written permission for release. With the exception of basic certification information and results of testing for pesticide residues and other prohibited substances,

your organic certifier is not permitted to disclose other information about your operation unless you have permitted it in writing.<sup>25</sup> According to the NOP regulations, organic certifiers must “maintain strict confidentiality” with respect to farmer clients and must not disclose to third parties any business-related information obtained during the organic certification process.<sup>26</sup> However, certifiers are permitted to disclose business-related information if permitted in writing by the farmer.<sup>27</sup>

To some extent, then, the NOP regulations allow the farmer to decide what the certifier can release to a buyer. To limit the information about your operation that the buyer can get from the certifier (which you may want to do to ensure the buyer does not access sensitive, extraneous, or confidential information), you could ask the buyer what information it needs and then agree in writing only to the release of that specific information.

#### Don't Make Promises for Your Certifier

It is unwise to agree to contract language promising that an organic certifier will directly provide a buyer with any information. As a general rule, it is risky to make contract promises on behalf of a certifier (or anyone else) who is not a party to the contract. This is risky because you cannot be sure a certifier will release records according to the buyer's wishes. For example, you could end up in a situation where the certifier fails to provide the buyer with access or notifications, even if you have signed a release allowing the certifier to do so. At minimum, therefore, if your buyer insists that you allow direct access to certifier records, do not promise anything to the buyer beyond your agreement to the certifier's release of specific information.

#### You Can Require Copies

To ensure you are kept informed about what information the certifier is sending the buyer, you could include language in the contract requiring that the buyer send you copies of any records released to the buyer by your certifier regarding your farm operation.

**Example: Limited Access to Certifier Records Provision**

Seller agrees that Organic Certifier may release to Buyer copies of Seller's records directly related to non-compliance investigations, proposed suspensions or revocations of certifications, or other violations of the NOP regulations. Organic Certifier may release the above records only for the current or past calendar year unless Seller has given advance written permission. Additionally, Seller does not agree to the release of sensitive and/or confidential information by Organic Certifier to Buyer without Seller's advance written permission. Furthermore, Buyer agrees to provide Seller with copies of any records released by Organic Certifier regarding Seller within 15 business days of receipt.

**Does the contract address “split operations” or the presence of non-organic crops or animals?****NOP Regulations on Split Operations**

The NOP regulations allow farms to be “split operations,” meaning part of the farm is certified organic, while another part of the farm produces non-organic crops, dairy or livestock.<sup>28</sup> Farmers with split operations must take steps to prevent commingling, and must use adequate measures to segregate organic from non-organic crops and production inputs.<sup>29</sup> Accordingly, organic certifiers can inspect the non-organic side of the farm operation to ensure it is not compromising the organic portion of the farm, and farmers with split operations must include in their OSP a description of the measures the farmer has established to prevent commingling and organic crop contact with prohibited substances.<sup>30</sup>

**Beware of Contract Prohibitions on Split Operations or Presence of Non-Organic Animals or Crops**

Even though most certified organic buyers are themselves split operations handling both organic and non-organic products, some buyers include provisions in organic contracts prohibiting farmers from running split operations. Some buyers go even further, prohibiting any presence of



non-organic, cloned, or GMO animals or crops on the contracting farm. If you do not run a split operation, this requirement might not seem problematic. However, even if you run an organic-only operation, you might unintentionally run into trouble with this prohibition if animals have to be transitioned out of organic production (for example, for health reasons), or if fields become ineligible for organic certification (for example, due to floodwater contamination). Additionally, most organic farmers will have non-organic crops on their farms in the form of buffer crops. Many will have fields or animals transitioning to organic.

Clearly, then, it is best not to sign a contract prohibiting the presence of any non-organic animals or crops on your farm. If your buyer is concerned about commingling or contamination, you could offer to keep records of non-organic commodity movement (conventional, buffer, and transitional) and make them available to the buyer on a regular basis.<sup>31</sup> Additionally, you could make available records of steps you have taken to ensure organic integrity.



#### **Create Exception for Buffer Crops, Transitional Products**

If a buyer insists on a contract provision prohibiting any non-organic commodities on the farm, and you are willing to comply, consider (at minimum) including an exception for buffer crops, transitional crops or animals, and nonorganic crops or animals present on your farm for reasons beyond your control.

#### **Does the contract provide support for an organic transition?**

Some organic buyers provide financial support to farmers during the three-year organic transition process. For example, some contracts include higher-than-conventional transition prices or lump-sum payments for farmers transitioning from conventional production to organic production. While this is an admirable practice that supports new organic farmers, be aware of whether the contract requires you to repay any transitional support if your farm fails to attain certification after three years. If such a requirement is triggered, you could be forced to repay a significant sum of money. Also, the transition payments, while helpful, are unlikely to cover the entire cost of transitioning to a new system of farming.

### Exclusivity Required?

Be particularly aware of any strings attached to transition support provided by the buyer. For example, you might have to agree that for some period of time post-transition you will only sell your organic products to the buyer who provided transition support. Make sure you are willing to continue the contract relationship for that extra period of time.

#### **Add an Exclusivity Escape Clause**

Note that, while you may have to agree to sell only to the buyer who provided transition support, the buyer is unlikely to promise to purchase all of your organic production during that time (due to the buyer's desire to maintain flexibility in case the market becomes over-supplied). Thus, you could end up in a situation where you have promised to sell only to one buyer, but that buyer won't purchase your organic product. You may wish to include contract language stating that if the buyer refuses to purchase your product for any reason, you can sell the product to another buyer without penalty.



### Don't Go Organic Just Because of Transition Support

It may be wise to consider whether demand for your newly transitioned organic product is likely to remain strong after you achieve organic certification. Organic buyers often offer transition support as an incentive for farmers when demand for a certain commodity exceeds supply. However, organic supply and demand relationships often fluctuate, leading to periods of oversupply and low prices (for example, organic dairy in 2008-2009).<sup>32</sup> Although you cannot predict the future, be cautious about entering the organic market just for the transition payments. If you are committed to organic production for the long term, transition payments are very valuable; but if you are only looking for short-term gain, the transition may not be cost-effective even with the transition support.

### Premium Pricing

Instead of providing direct support for the transition to organic, some buyers will pay a premium price for transitional products. The premium is

unlikely to equal the organic premium that buyer offers, but would likely be higher than the conventional price. If your contract includes a transitional premium, the contract should make clear whether it is tied to the conventional price (conventional price plus some amount) or the organic price (organic price minus some amount). Depending on your transitional commodity, one formula may be significantly more profitable for you.

#### Verification of Transitional Status

Finally, does the contract address how your transitional status will be verified? You may wish to negotiate a verification process to protect yourself against any claim by the buyer that your farm is not making satisfactory progress in the transition. On the other hand, you may not want to make the transition process more difficult by adding additional paperwork requirements for yourself.

**CHAPTER 8 – ENDNOTES**

- <sup>1</sup> See 7 C.F.R. §§ 205.662 (non-compliance), 205.663 (mediation), 205.681 (appeals) (2012).
- <sup>2</sup> See 7 C.F.R. § 205.681 (2012). There have been bills proposed in Congress that would change NOP enforcement procedures and eliminate the stay associated with an appeal. However, at the time this guide was printed, none of these proposals had been adopted.
- <sup>3</sup> See U.C.C. § 2-609 (1977) (“Right to Adequate Assurances”).
- <sup>4</sup> See 7 C.F.R. § 205.671 (2012).
- <sup>5</sup> See 7 C.F.R. § 205.670(b) (2012).
- <sup>6</sup> See 7 C.F.R. §§ 205.2, 205.105, 205.272, 205.600, 205.602, 205.604 (2012).
- <sup>7</sup> See 7 C.F.R. § 205.2 (2012). The NOP regulations define “excluded methods” as: “[a] variety of methods used to genetically modify organisms or influence their growth and development by means that are not possible under natural conditions or processes and are not considered compatible with organic production. Such methods include cell fusion, microencapsulation and macroencapsulation, and recombinant DNA technology (including gene deletion, gene doubling, introducing a foreign gene, and changing the positions of genes when achieved by recombinant DNA technology). Such methods do not include the use of traditional breeding, conjugation, fermentation, hybridization, in vitro fertilization, or tissue culture.” See Lynn A. Hayes, *Farmers’ Guide to GMOs*, at 54 (Farmers’ Legal Action Group, 2d ed. 2009), available at <http://flaginc.org/topics/pubs/arts/FGtoGMOs2009.pdf>.
- <sup>8</sup> See 7 C.F.R. §§ 205.600-606 (2012).
- <sup>9</sup> See Center for Environmental Risk Assessment, *GM Crop Database*, available at [http://cera-gmc.org/index.php?action=gm\\_crop\\_database](http://cera-gmc.org/index.php?action=gm_crop_database).
- <sup>10</sup> See 7 C.F.R. § 205.2 (2012). The NOP regulations define “excluded methods” as: “[a] variety of methods used to genetically modify organisms or influence their growth and development by means that are not possible under natural conditions or processes and are not considered compatible with organic production. Such methods include cell fusion, microencapsulation and macroencapsulation, and recombinant DNA technology (including gene deletion, gene doubling, introducing a foreign gene, and changing the positions of genes when achieved by recombinant DNA technology). Such methods do not include the use of traditional breeding, conjugation, fermentation, hybridization, in vitro fertilization, or tissue culture.” GMOs are deemed an “excluded method” in organic production. See Lynn A. Hayes, *Farmers’ Guide to GMOs*, at 54 (Farmers’ Legal Action Group, 2d ed. 2009), available at <http://flaginc.org/topics/pubs/arts/FGtoGMOs2009.pdf>.
- <sup>11</sup> See 7 C.F.R. § 205.272 (2012); see also Lynn A. Hayes, *Farmers’ Guide to GMOs*, at 53-54 (Farmers’ Legal Action Group, 2d ed. 2009), available at <http://flaginc.org/topics/pubs/arts/FGtoGMOs2009.pdf>.
- <sup>12</sup> See *Organic Seed Growers and Trade Ass’n v. Monsanto Co.*, 11 Civ. 2163 (NRB), 2012 WL 607560 (S.D.N.Y. February 24, 2012).

- <sup>13</sup> Non-GMO Project, *GMO Testing Guidelines* (2012), available at <http://www.nongmoproject.org/industry/about-gmo-testing/guidelines/>.
- <sup>14</sup> See Jim Riddle, *GMO Contamination Protection: What Does it Take?*, available at [http://swroc.cfans.umn.edu/prod/groups/cfans/@pub/@cfans/@swroc/documents/article/cfans\\_article\\_390283.pdf](http://swroc.cfans.umn.edu/prod/groups/cfans/@pub/@cfans/@swroc/documents/article/cfans_article_390283.pdf).
- <sup>15</sup> See 7 C.F.R. §§ 205.201, 205.272 (2012).
- <sup>16</sup> See 7 C.F.R. §§ 205.201, 205.272 (2012).
- <sup>17</sup> See National Sustainable Agriculture Information Service (ATTRA), *Forms, Documents and Sample Letters for Organic Producers* (2005), available at <https://attra.ncat.org/attra-pub/viewhtml.php?id=170> (providing templates for equipment cleaning log, clean transport affidavit, buffer crop disposition records, sample neighbor notification letter, and adjoining land use verification). If the contract requires you to maintain an equipment clean-out log, the ATTRA website has a free template for download at <https://attra.ncat.org/attra-pub/OrganicFieldDocForms/1P.xls>.
- <sup>18</sup> See 7 C.F.R. §§ 205.240, 205.2 (2012).
- <sup>19</sup> See 7 C.F.R. § 205.239 (2012).
- <sup>20</sup> See 7 C.F.R. § 205.239 (2012).
- <sup>21</sup> See 7 C.F.R. §§ 205.2 (commercially available), 205.204 (seeds and planting stock practice standard) (2012).
- <sup>22</sup> This is sometimes informally referred to the “3-source” rule—meaning that you should document that you attempted to obtain organic seed from three sources prior to deeming the organic seed commercially unavailable. However, the NOP regulations make no reference to the number of organic sources required; it could be more or less than three, depending on the circumstances.
- <sup>23</sup> See 7 C.F.R. § 205.204(a) (2012).
- <sup>24</sup> See National Sustainable Agriculture Information Service (ATTRA), *Forms, Documents and Sample Letters for Organic Producers* (2005), available at <https://attra.ncat.org/attra-pub/viewhtml.php?id=170>.
- <sup>25</sup> See 7 C.F.R. § 205.504(b)(5) (2012). Entities seeking organic certifier accreditation must submit the following: “A copy of the procedures to be used, including any fees to be assessed, for making the following information available to any member of the public upon request: (i) Certification certificates issued during the current and 3 preceding calendar years; (ii) A list of producers and handlers whose operations it has certified, including for each the name of the operation, type(s) of operation, products produced, and the effective date of the certification, during the current and 3 preceding calendar years; (iii) The results of laboratory analyses for residues of pesticides and other prohibited substances conducted during the current and 3 preceding calendar years; and (iv) Other business information as permitted in writing by the producer or handler.”
- <sup>26</sup> See 7 C.F.R. § 205.501(a)(10) (2012); see also National Organic Program, Instruction, *Disclosure of Information Concerning Operations Certified*

*Under the National Organic Program* (November 23, 2011), available at <http://www.ams.usda.gov/AMSV1.0/getfile?dDocName=STELPRDC5088941>.

- <sup>27</sup> See 7 C.F.R. § 205.504(b)(5) (2012); see also National Organic Program, Instruction, *Disclosure of Information Concerning Operations Certified Under the National Organic Program* (November 23, 2011), available at <http://www.ams.usda.gov/AMSV1.0/getfile?dDocName=STELPRDC5088941>.
- <sup>28</sup> See 7 C.F.R. § 205.2 (2012).
- <sup>29</sup> See 7 C.F.R. § 205.272 (2012).
- <sup>30</sup> See 7 C.F.R. § 205.201(a)(5) (2012).
- <sup>31</sup> National Sustainable Agriculture Information Service (ATTRA), *Documentation Forms for Organic Crop and Livestock Producers* (2011), available at <https://attra.ncat.org/attra-pub/summaries/summary.php?pub=358>.
- <sup>32</sup> See Farmers' Legal Action Group, *Tools for Dairy Farmers in Tough Economic Times* (November 2010), available at <http://flaginc.org/topics/pubs/arts/DairyNov2010pdf.pdf>.

# 9

## Beyond Organic

- [9-1](#) Does the contract require you to go beyond NOP regulations?
- [9-3](#) Does the contract require you to produce organic farm products that satisfy marketing claims in addition to “certified organic”?
- [9-5](#) Does the contract require your farm to look “pleasing”?
- [9-6](#) Does the contract require unspecified “best management practices”?
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### CHAPTER QUICK TIP

#### **Incorporated Buyer Policies Have the Same Force as Contract Provisions**

Generally speaking, any policies or documents the contract refers to as “incorporated” into the agreement are part of the contract and have the same force and effect as any other contract provision. Breach of any part of an incorporated policy is the same as breach of the contract. Thus, if you agree to an incorporated policy, you are also promising to follow the requirements of that policy.







## **DOES THE CONTRACT REQUIRE YOU TO GO BEYOND THE NOP REGULATIONS?**

All of the topics covered in this chapter are related to contract requirements that go above and beyond the requirements necessary for organic certification. If the contract agreement is simply for “certified organic” products, it should be clear that the farmer is only required to comply with the National Organic Program (NOP) regulations.



### Example: Products Will Be Organic

All products covered under this contract will be produced in compliance with NOP regulations.

However, if you agree to provide products that are not only certified organic but also go beyond organic (by, for example, taking additional steps in the production process), it is important for the contract to clearly define any requirements that are in addition to NOP regulation requirements. This is necessary for you to be sure that you understand what the buyer is expecting. When complying with your Organic System Plan (OSP) might not be enough to keep you in compliance with the contract, you will need the contract itself to set out what else is required.

For example, the contract might require compliance with international organic standards (such as Japan’s), you could be required to provide minimum square feet of space per chicken indoors and outdoors, you might agree not to use certain inputs that are allowed under NOP regulations (such as sodium nitrate), or you might agree not to use oxytocin even for emergency purposes. Each of these requirements would go beyond what is required for organic certification.

### Beware of Mistaken Buyer Beliefs About “Certified Organic”

As part of making sure that requirements beyond those for organic certification are clearly set out in the contract, you should talk with the buyer about what “certified organic” actually means for your operation and farm products. Some buyers may mistakenly believe “certified organic” means more than it actually means, and so may not consider their expectations to be “beyond” organic. As discussed in Chapter 8, certified organic does not mean 100 percent GMO-free; it does not mean grass-finished, it does not mean free-range, it does not mean 100 percent pesticide-free, and it does not even mean synthetic-free. Certified organic simply means produced in compliance with the federal organic standards established by the NOP.<sup>1</sup> Not all buyers will understand the limited meaning of “certified organic,” and may contract for your organic commodities under the mistaken belief that organic means something different. This misunderstanding could be dangerous.

For example, a buyer expecting 100 percent pesticide-free wheat might reject your delivery as not satisfying the contract if testing shows some pesticide residues, even if the residues are less than the tolerance permitted by the organic rules. You could argue that the buyer should accept your wheat under the contract because it meets the organic standards; but if the buyer refuses, your only remedies might be expensive litigation or arbitration.

Avoid surprise buyer rejections by: (1) clearly communicating with the buyer about the meaning of “certified organic”; and (2) clearly setting out in the contract what additional measures you will have to take, if any, to simultaneously comply with federal organic regulations and the contract obligations.



## MARKETING CLAIMS

### **Does the contract require you to produce organic farm products that satisfy marketing claims in addition to “certified organic”?**

Buyers may wish to market their products with claims in addition to organic, such as grass-fed, grass-finished, free range, biodynamic, humanely raised, open-pollinated, GMO-free, fair trade, or locally grown. If the contract requires you to produce an organic product that also satisfies one or more of these additional marketing claims, you will want to make sure that both you and the buyer are working from the same definition. Consider including the definition of the marketing claim in the contract. This can be harder than it sounds, because although some of these claims have at least some legal definition, some mean entirely different things to different people.

Also, do any of these required marketing claims require additional certification? If so, you should know the certification process, paperwork, and costs before signing the contract.

Some buyers contract for organic farm products that are in compliance with both federal organic standards and additional social justice certification programs. Examples include fair trade goods (domestic and international) and goods produced in compliance with Agricultural Justice Project standards ([www.agriculturaljusticeproject.org](http://www.agriculturaljusticeproject.org)).

### **Complying with Additional Marketing Claims**

If the contract requires you to comply with additional marketing claims and/or social justice standards, be sure that you:

- Fully understand how your production methods must change or expand in order to comply with both organic requirements and requirements that go beyond organic.
- Obtain a copy of any additional standards required by the contract.
- Read the standards closely and determine what new requirements you must satisfy.

- Consider contacting representatives from an applicable marketing or social justice standards organization for help with compliance.
- Make sure to communicate with your organic certifier to ensure your new obligations do not interfere with your organic certification.
- Try to estimate the cost of compliance with the additional requirements and factor that cost into your consideration of whether the contract will be profitable.



## VAGUE AND SUBJECTIVE CONTRACT REQUIREMENTS

Organic contract requirements that go beyond what is required for organic certification often include somewhat fuzzy language about how farms should be operated and even what farms should look like. These types of requirements can be problematic both because they are unclear and because whether they are satisfied is often a matter of taste or opinion.

### **Does the contract require your farm to look “pleasing”?**

The organic contract may address your farm’s visual appearance. For example, the contract might state that your farm must be “kept in an aesthetically pleasing condition.” If you are offered a contract with such a provision, you may wish to ask the buyer whether it is really necessary; you may be able to delete it.

### **Subjective Provisions Increase Risk**

Provisions related to visual appearance, which may seem reasonable at first glance, can be risky because they are frequently vague and subjective. What might be “aesthetically pleasing” to one person may not be pleasing to another. Thus, because it is impossible to know exactly what your farm must look like in order to satisfy the requirement, it is easy to breach this kind of provision without realizing it.

Contract promises that are easy to breach are especially dangerous when they appear in a contract under which even minor breaches are grounds for cancellation (see Chapter 5, pages 5–4 through 5–7, for a discussion of blanket breach provisions). In this way, vague provisions about appearance provide an “easy out” for a buyer who decides it does not want to honor the organic contract. Consequently, you may wish to negotiate the deletion of this type of provision.

### **Possible Compromise — Specific Obligations**

If it is not possible to eliminate the appearance provision completely, you may be able to work out a compromise that gives specific, objective standards for you to meet. Ask the buyer why it is concerned with the farm’s appearance and then determine what actions would need to be

taken to maintain that desired appearance. This means you could agree to more specific obligations regarding farm upkeep, such as contract language promising that “trash will be promptly removed from the front yard of the farmhouse,” or “consistent with organic production practices, the farm will be kept reasonably free of weeds.” Agreeing to more specific obligations makes it more difficult for the buyer to claim that you breached the contract, but it also means that you will have to undertake these specific tasks or risk breach.

### **Does the contract require unspecified “best management practices”?**

As with requirements related to the farm appearance, vague and subjective language about “best management practices” can be dangerous, leaving the farmer vulnerable to an unexpected objection from the buyer or even contract termination. What does it mean to use best management practices on your farm? Two organic farmers could easily come up with two different answers. Does it simply mean adhering to the letter of the organic regulations? Does it mean compliance with a certain organic group’s idea of the spirit of organic? It is impossible to tell from the phrase “best management practices” alone.

Because a contract requiring you to use unspecified “best management practices” leaves a wide opening for the buyer to claim that you are in breach, it is wiser not to agree to such a provision. Instead, you could agree to specific management practices desired by the buyer, such as certain recordkeeping practices, integrated pest management (IPM), or annual audits. Alternatively, you could agree to practice “good organic management practices in compliance with NOP regulations,” or to operate in accordance with a published standards document specific to organic crops or livestock, such as the University of Minnesota’s Organic Risk Management Guide.<sup>2</sup>



## INSPECTION

### **Does the contract allow the buyer to inspect the farm?**

If the contract allows the buyer to inspect the farm, the buyer's right of access should be limited to some degree. It is understandable that a buyer would wish to see the farm, especially during the growing season, but unlimited access to farm property is probably unnecessary.

#### **Suggested Limitations on the Buyer's Right of Inspection Include:**

- *Require prior notice of inspection.*

Allowing an inspection “at any time” gives the buyer the right to inspect the farm even at inconvenient times, such as during the evening, on holidays, or when the farmer is absent. Requiring that the buyer give advance notice of an inspection is a reasonable limitation that you may wish to negotiate. The notice required could be a specific length of time, such as 36 hours prior to inspection, or a less predictable but still somewhat limited “reasonable notice” standard.

The contract could further state that notice has to be given in a certain way (by phone, by mail, by email, etc.). If the buyer is particularly concerned about seeing the farming operation without the changes and preparations that might come from advance notice, and the farmer is comfortable with the idea, a compromise could be to agree to a small number of “surprise” inspections.

- *Create reasonable inspection timeframes.*

You may be uncomfortable with a contract that allows the buyer to show up in the middle of the night or on the 4th of July (for example, language stating the buyer “may inspect at any time”). Consider limiting inspections to business or daylight hours, non-holidays, or days of the week you are usually working on the farm.

- *Limit the scope of the inspection.*

You may also be uncomfortable with a contract allowing the buyer access to parts of your farm unrelated to your organic farming

operation and contracted crop acres. A contract stating that the buyer shall have “unlimited access to the organic farm for purposes of inspection” would arguably allow the buyer to inspect any part of the farm, including personal living spaces. If the contract allows unlimited access and you block the buyer from inspecting some part of your farm – even a personal living area – you could be in violation of the contract. Thus, you may wish to negotiate language stating that inspections are limited to those buildings and areas closely related to the organic farming operation and contracted crop acres.

- *Accompany the buyer.*

You may wish to negotiate for the right to accompany the buyer on the inspection of your farm. It could be risky for the buyer to come onto your land unsupervised and perhaps even take samples without your knowledge. An unaccompanied buyer inspecting your farm could disturb growing crops or livestock, interfere (even unintentionally) with on-going projects, or even be injured. In addition, without farmers' supervision and guidance, buyers could misunderstand what they see on your farm and how it relates to the product they have contracted for. For example, a buyer might mistake a buffer area for an organically managed crop; if the buyer happened to sample the buffer area, it could mistakenly believe your crop has been contaminated and try to cancel the contract.

Some organic contracts might actually require farmers to accompany buyers during inspections. If so, it is even more important to require advance notice of inspection and a reasonable time frame for inspection (such as during business hours) so farmers are sure to be available and able to satisfy this requirement.

- *Limit the frequency of inspections.*

If a contract allows a buyer to inspect the farm at will, the buyer could theoretically conduct an inspection multiple times a day, every day of the year—or at least often enough to be disruptive. Consider limiting inspections to a certain number or a certain number per unit of time (once a month, once per season, etc.).





## INCORPORATED BUYER POLICIES AND LAWS

### **Does the contract incorporate separate buyer-created policies?**

Generally speaking, any policies or documents that the contract refers to as “incorporated” into the agreement are part of the contract and have the same force and effect as any other contract provision. Therefore, it is very important to read and understand any buyer-created policies that may be incorporated into your organic contract.

Buyer policies can become part of a contract if they are completely restated in the body of the contract, or if they are “incorporated by reference,” which means that contract language simply mentions the separate policy and states the intent for the policy to be a binding part of the contract. There is no requirement that the separate policy be presented to you prior to signing the contract for an incorporation by reference to be binding. Note that an incorporated policy could easily be longer and more complicated than the contract itself.



#### Example: Incorporation of Additional Policies

Attachment A (Premium/Discount Table), Attachment B (Buyer’s Quality Standards), and Attachment C (Buyer’s Production Policy) attached to this Agreement are hereby incorporated into and made a part of this Agreement.

#### Or:

Producer agrees to produce, harvest, and store the contracted organic crop in compliance with the most up-to-date standards accepted and promulgated by Buyer.

If the contract incorporates a policy created by the buyer, you may wish to take some or all of the following steps to protect yourself from potentially burdensome and unexpected legal obligations:

- Obtain a full, current copy of any buyer-created policy, standard, or other document incorporated into the contract. Don't sign the contract until you have obtained and read the policy.
- Read the policy before signing the contract and apply the same scrutiny to the policy as you did to the main contract. That means you should ask all of the same questions about the policy as you would have asked if the policy language were actually written in the contract. Consider whether you want to negotiate contract language that cancels out some parts of the policy. Take as much time as you need to review the policy; if you sign the contract, you are also promising to carry out the policy requirements—which could be costly and difficult.
- Identify any areas of conflict or inconsistency between the contract and the policy. For example, the contract might include a 30-day delivery window but make no mention of a penalty for late delivery. The policy, in contrast, might state that the buyer receives a one percent discount for every day the delivery is late. If you find inconsistencies like this, discuss the situation with the buyer and request that the conflict be resolved in the contract before signing.



### **Suggestion for Resolving Conflicts Between Contract and Incorporated Policies**

As a potential solution in case of conflict between the contract and an incorporated policy, consider adding language to the contract stating “if the policy conflicts with the contract, the contract language controls.”

Note that just stating that the contract language controls policy requirements might not protect you in all cases. For example, in cases where the policy adds requirements that do not conflict with the contract, but are in addition to the contract (like the one percent discount penalty example on the previous page), there is an interpretation where the contract and the policy could co-exist and be in effect without conflict.

So, if the policy adds obligations that you are uncomfortable with or believe are unclear, consider negotiating alternative policy language or contract language that clearly sets out your understanding of the particular obligation. You could also ask the buyer to clarify the situation by putting the policy and the contract into a single document instead of incorporating the policy by reference. When everything is in one document, obligations can become clearer, inconsistencies may be uncovered more easily, and it might be easier to negotiate changes.

- Watch out for language in an incorporated policy stating that the policy “supersedes” or “controls” in case of conflict with the contract. (In general, you will want the contract to supersede the policy, not the policy to supersede the contract.) If the policy supersedes, you must consider the text of the policy to be your main agreement with the buyer. If this makes you uncomfortable, consider asking for deletion of the “superseding” language.
- Be especially careful if the contract allows termination for even minor contract breach (blanket breach) (see Chapter 5, pages 5–4 through 5–7). Breach of any part of an incorporated policy is the same as breach of the contract, so vague and subjective terms in an incorporated policy are just as dangerous as vague and subjective terms in the contract.

### **Does the contract incorporate specific federal, state, or local laws?**

Buyers sometimes include contract language stating that farmers will comply with specific statutes or regulations or even “all applicable laws.” Since most farmers are presumably intending to comply with the laws of the nation, state, and locality—whether or not those laws are incorporated into the contract—such a provision may not seem very important. However, this type of provision can create significant risks for farmers, particularly if the contract has a provision allowing the buyer to cancel the contract for any breach by the farmer, no matter how insignificant (blanket breach, discussed in Chapter 5, pages 5–4 through 5–7).

Because statutes and regulations are constantly changing, even a farmer who is making an effort to be in full compliance may not be up-to-date on current requirements. Also, laws are often unclear, and their meaning can be open to dispute and further interpretation by the courts. Thus, a buyer might say that a farmer is in violation of a specific incorporated law and therefore in violation of the contract based on the buyer’s understanding of what is required, but that might not be the only, or even the most common, interpretation. A farmer in that situation might have to hire an attorney and dispute the buyer’s interpretation in court or in private arbitration.

Additionally, the many statutes and regulations applicable to a typical farm represent hundreds if not thousands of possible violations of a contract that incorporates a requirement that a farmer comply with applicable law. Even if the law incorporated into the contract is limited to a specific statute or regulatory program, there will likely be many very minor requirements of which violation could be considered a breach of the contract. In many cases, particularly for laws governing farms, the punishment for violation of a law is simply that farmers make up the defect and pay a fine to the government. Enforcement agencies recognize that it would be significant overkill to shut down an operation for minor violations; but contract language making any legal violation a breach of the contract could threaten just that.

If the contract you are offered incorporates specific laws or states a requirement to apply with all applicable law, consider asking the buyer to delete the language, since you intend to follow the law anyway. Alternatively, instead of incorporating an entire law into the contract, you could suggest a provision stating that “major violations” of “relevant laws” could be grounds for contract cancellation. If the final contract language does incorporate laws, before signing ask the buyer for a copy of the laws mentioned in the contract.



## FOOD SAFETY AND NANOTECHNOLOGY

### **Does the contract address food safety practices?**

As food safety has become a hot national issue, buyers are increasingly addressing food safety practices in organic contracts. As with all contract obligations, you should be sure that you are prepared to meet any food safety requirements, that you can comply and still make an acceptable profit from the contract, and that the buyer's food safety requirements are not in conflict with the NOP regulations.

### **Food Safety Obligations That May Appear in Organic Contracts Include:**

- *Traceback*

The organic contract could include obligations that are intended to ease “traceback,” or the ability to track food items back to their source. Traceback can be useful in preventing the spread of foodborne illnesses, as the source of the outbreak can sometimes be identified and contained. Traceback can also protect farmers by enabling them to prove that their farm was not the cause of an outbreak. Additionally, traceback can be used as a marketing mechanism. Consumers may be more interested in purchasing a particular food item if they know which farm produced the raw materials for that item.

Farmer obligations related to traceback may require practices such as livestock ID tags, shipment affidavits, stickers, bar codes, and product lot numbers, all of which are standard practice to maintain organic certification.

- *Recall*

Large-scale food recalls have, unfortunately, become relatively commonplace in recent years. These recalls are often quite damaging to the reputations of companies whose products are recalled. As a result, some buyers are including provisions related to recall procedures in organic contracts.

As a farmer, you may be concerned about the scope of the buyer's control over the recall process. For example, if the contract gives the buyer the right to control everything about the recall,

including any public statements to be made on the matter, your voice could be entirely silenced. That means if the buyer is inclined to blame your farm for the food safety issue, you will have contracted away your right to publicly dispute the buyer's claims. And if you decide to make a public statement in spite of the contract (in order to protect your farm's reputation), the buyer could sue you for the harm your statements might cause.

Additionally, the contract may require you to take all steps ordered by the buyer in case of a recall. These steps could be costly, or even unnecessary in your view, but if you agree to follow the buyer's orders in a recall situation, you will have agreed to take on whatever duties the buyer wants. Your idea of what should be done and a larger company's idea of what should be done may differ considerably.

That said, if the buyer insists on including language related to recall procedures in the organic contract, consider negotiating language such as, "In case of recall, Buyer and Seller agree to make best efforts to create a mutually acceptable recall strategy." This kind of broad language gives you more flexibility in case you and the buyer end up on opposing sides during a recall.

- *Good Agricultural Practices (GAPs)*

The major institutionalized food safety certification program for farmers is the Good Agricultural Practices (GAP) audit program. The GAP program focuses on best agricultural practices to verify that farms selling fruits and vegetables are producing them in a safe manner. The program's goal is to minimize the risks of microbial food safety hazards by addressing the following categories: water, manure and municipal biosolids, worker health and hygiene, sanitary facilities, field sanitation, packing facility sanitation, transportation, and traceback. If the contract requires you to participate in the GAP program, be sure to obtain a copy of the program requirements and understand your obligations before signing the contract.

- *Compliance with state and local food safety laws*

Organic contracts might require compliance with state and local food safety laws and regulations, including licensing requirements. Make sure you understand these requirements, and see pages 9–9 through 9–12 of this chapter for a discussion of the risks of contracts that incorporate laws.

- *Compliance with marketing agreements on food safety*

Marketing agreements among buyers related to food safety have been implemented in at least two states. Moreover, the U.S. Department of Agriculture (USDA) has also proposed a national food safety-related marketing agreement, to be called the National Leafy Greens Marketing Agreement, which has not yet been put in place. Organizations that promote organic and sustainable farming are concerned that marketing agreements like these create a bias toward chemically intensive, environmentally damaging, mono-cultural farming practices and thus, in the name of food safety, promote conventional farming practices and penalize organic farmers.<sup>3</sup>

USDA's national proposal is modeled after the California Leafy Greens Marketing Agreement. The California agreement was established in 2007 by a group of California leafy greens handlers in response to the September 2006 *E. coli* outbreak attributed to California spinach greens. The agreement promotes chemical fertilizers and makes it more difficult to use the non-synthetic, natural nutrient sources common in organic production. Additionally, the California agreement also provides a strong incentive for farmers to remove wildlife habitat bordering growing areas, in stark contrast to the federal organic standards, which require organic growers to promote biodiversity. The wildlife habitat destruction also impedes organic farmers' ability to provide habitat for the beneficial insects that are commonly a part of many organic farms' non-chemical pest management strategies.

Although the current California agreement and the proposed USDA agreement are implemented at the buyer level and are not technically required for farmers, in practice farmers may find that the requirements work their way down the line to them through contract obligations. When farmers are unable to find a buyer who does not require through contract that the farmer satisfy the marketing agreement standards, those standards have essentially become farmer requirements.

Still, farmers should be very hesitant to sign a contract with a buyer that is a party to the California Leafy Greens Marketing Agreement or any similar agreement in another state. The requirements of the marketing agreement are very likely to conflict with the farmer's OSP, potentially placing the farmer's organic certification in jeopardy.

- *Product liability insurance*

As discussed in Chapter 4, pages 4–17 and 4–18, organic contracts may require farmers to obtain insurance. In the food safety context, the important type of insurance is product liability insurance. Even if you already have farm-related commercial liability insurance, check to see whether it includes product liability coverage. If not, talk with your insurer about whether you can tailor your policy to include product liability coverage or obtain a separate product liability policy. Be aware that a contract provision requiring product liability coverage probably will not be waived if you find that coverage is unexpectedly expensive or unavailable from your preferred insurance provider.

### **Does the contract address nanotechnology?**

Nanotechnology is the process of manipulating matter on an atomic and molecular scale and deals with developing materials sized in the range of 1 to 100 nanometers. As one nanometer equals one one-billionth of a meter, these nanomaterials are obviously extremely small. Nanomaterials, which exist in computers and other electronics, textiles, cosmetics, chemicals, and food, are increasingly present in commercial materials. However, due to a lack of regulation in this area, it is nearly impossible to tell whether a particular item contains engineered nanomaterials.

Currently, there are no organic regulations governing the presence of nanomaterials in organic food or processing. In late 2010, however, the National Organic Standards Board (NOSB) recommended that the NOP create regulations prohibiting nanomaterials from organic production.<sup>4</sup> Concerns related to nanomaterial contamination of organic production involve all stages of production of an organic product, including growing, processing, and packaging. The most significant concern with respect to organic production is contamination from primary packaging and food contact surfaces. Although nanomaterials may be difficult to regulate, it is likely that the NOP will create regulations related to nanotechnology in the not-too-distant future.

### **Advisable to Delete Contract Language on Nanomaterials**

Despite the absence of current regulation and the difficulties with detection of and protection against nanomaterials, it is possible that the organic contract could include language related to nanomaterials. If so, remember that simply following the NOP regulations will not be enough to ensure that your organic commodities remain nanotech-free. Nanotechnology can be found in fertilizer, pesticides, packaging, water, feed, and many other agricultural inputs. Most will not even be labeled as



containing nanomaterials. Consider how you would go about ensuring that the materials you use in organic production would not become contaminated with nanomaterials, and whether it would be cost-effective to do so. For the present, due to the difficulty of determining whether a particular material contains nanotechnology, it is advisable to delete any contract language requiring your organic farm products to remain free of nanomaterials. Alternatively, you could agree to use “best efforts” to avoid nanomaterials or agree to “not knowingly use” nanomaterials. Or, you could agree to comply with the NOP regulations as they relate to nanotechnology.

**CHAPTER 9 – ENDNOTES**

- <sup>1</sup> 7 C.F.R § 205.2, “Organic” (2012).
- <sup>2</sup> See generally, Mary P. Brakke, *et al.*, *Organic Risk Management Guide* (Kristine M. Moncada and Craig C. Sheaffer, eds., Regents of the University of Minnesota, 2010), available at <http://www.organicriskmanagement.umn.edu>.
- <sup>3</sup> National Organic Coalition, Media Release, *National Organic Coalition Disappointed Over USDA Decision to Move Forward With Leafy Greens Marketing Agreement*, April 26, 2011; see also, Shermain D. Hardesty and Yoko Kusunose, *Growers' Compliance Costs for the Leafy Greens Marketing Agreement and Other Food Safety Programs*, UC Small Farm Program Research Brief (University of California, September 2009), available at <http://sfp.ucdavis.edu/files/143911.pdf>.
- <sup>4</sup> National Organic Standards Board, Formal Recommendation by the National Organic Standards Board (NOSB) to the National Organic Program (NOP), *Guidance Document -- Engineered Nanomaterials in Organic Production, Processing, and Packaging* (October 28, 2010), available at <http://www.ams.usda.gov/AMSV1.o/getfile?dDocName=STELPRDC5087795>.

# 10

## Dispute Resolution

- [10-1](#) Where will the dispute be resolved?
- [10-2](#) Which state's laws should apply?
- [10-4](#) Does your contract require arbitration?
- [10-6](#) Does the contract require mediation of disputes?
- [10-7](#) Does the contract discuss who might have to pay attorney fees or costs?
- [10-8](#) Does the contract mention "liquidated damages" or other penalties?

### CHAPTER QUICK TIPS

#### **Arbitration Is Generally Bad For Farmers**

If a contract offer includes an arbitration provision, you should most likely try to delete it. Arbitration is often prohibitively expensive for farmers compared to public court actions. Arbitration provisions can be replaced with a provision stating that disputes will be resolved in the courts of your state.

#### **Try To Resolve Disputes In Your State**

If travel to the venue (place where disputes are resolved) selected in the contract is prohibitively expensive, it could prevent you from getting the benefit of legal remedies to which you might be entitled. Furthermore, it could prevent you from successfully defending a lawsuit if the buyer decides to sue you. If possible, it is best if the contract allows you to resolve disputes in your state.



# DISPUTE RESOLUTION

Many contracts contain provisions detailing what should happen in case of a dispute.

## Where will the dispute be resolved?

It is very common for a contract to include a provision selecting the geographical location or court where any dispute related to the contract must be decided. Sometimes the parties agree on a state where the disputes will be resolved, and sometimes they even agree on a specific district or county. The location of a legal dispute is often referred to as the “venue.”



### Example: Venue Provision

Venue of any legal proceeding related to the Agreement shall be in Dane County, Wisconsin.

Or:

All claims, disputes, and lawsuits arising out of or in connection with this Contract shall be resolved or adjudicated in the city of Houston in the State of Texas. The parties waive any jurisdictional or venue arguments to the contrary.

## Distant Venues Can Be a Problem

The venue, or the location where a dispute will be resolved, can be problematic for farmers if it is far away. The travel expenses associated with a lawsuit in a distant location can be very burdensome. Also, lawsuits can require a party to make frequent court appearances. Although judges

will sometimes allow appearances by phone for particular parts of the litigation, in-person appearances are generally required. Additionally, if you have hired a local attorney, you would likely have to pay for the expense of his or her travel to another state. You would probably also have to bear the expense if your attorney must associate with an attorney located in the state in which the dispute must be resolved (often required by courts for out-of-state attorneys).

If travel to the venue selected in the contract is prohibitively expensive, it could prevent you from getting the benefit of legal remedies to which you might be entitled. Furthermore, it could prevent you from successfully defending a lawsuit if the buyer decides to sue you.

**Example: Better Venue Provision**

All claims, disputes, and lawsuits arising out of or in connection with this agreement shall be resolved or adjudicated in the courts of the state where Grower either lives or farms.



### **Which state's laws should apply?**

Organic contracts often include language selecting which state's laws should be used to govern and interpret the meaning of the contract. These provisions are included in part to prevent or simplify court battles over which state's laws should apply. Additionally, a savvy buyer might pick a state with laws that are more business-friendly than farmer-friendly. For example, many corporations write contracts requiring disputes to be resolved under Delaware law because Delaware is famously friendly to corporations.

#### **Choice of Law**

The selection of which state's laws should apply in a dispute is often called "choice of law."



Example: Choice of Law

The parties expressly agree that this Agreement shall be governed by, interpreted under, and construed and enforced in accordance with the laws of the state of Delaware.

Or:

This Contract and incorporated documents are governed by and shall be construed in accordance with the laws of the state in which the products are to be delivered or the services are to be performed.

How Choice of Law Can Affect You

At the beginning of a lawsuit, the choice of law for a contract will likely affect you less than the choice of venue, because it is unlikely to add extra expense to the legal proceedings. However, the actual outcome of a contract dispute that ends up in court could be very different depending on which state's laws govern the contract. Therefore, you may want to think about whether you are willing to give up the protection of your state's laws if they are farmer-friendly. (See Chapter 12, pages 12–13 through 12–15, for a description of some state law protections for agricultural contracts.)

The contract might also say that a particular state's version of the Uniform Commercial Code (U.C.C.) applies to the contract. Please see Chapter 12, page 12–13, for a more thorough discussion of the U.C.C. and its relationship to each state.



Example: Better Choice of Law Provision

Governing Law: The parties expressly agree that this Agreement shall be governed by, interpreted under, and construed and enforced in accordance with the laws of the state where the Grower lives or farms.

## **Does your contract require arbitration?**

Arbitration is a decision-making process in which a person who is not involved in a dispute (an arbitrator) makes a decision after hearing from both sides. This decision is usually binding on the parties, and it generally may not be appealed to a state or federal court. Additionally, if you sign a contract with an arbitration clause, the buyer will generally be able to stop any public court proceedings you may initiate and have your lawsuit moved to private arbitration.

### **Example: Arbitration Provision**

The parties to this contract agree that the sole remedy for resolution of any and all disagreements or disputes arising under or related to this contract shall be through arbitration proceedings pursuant to the American Arbitration Association (AAA) rules. The decision and award determined through such arbitration shall be final and binding upon the Buyer and Seller. Judgment upon the arbitration award may be entered and enforced in any court having jurisdiction thereof.



By and large, binding arbitration clauses are bad for farmers. Binding arbitration limits the remedies available to farmers and usually prevents farmers from raising legal claims in state or federal courts. Moreover, arbitration can involve large fees that can altogether prevent farmers from pursuing their legal claims or rights under the contract. These fees can include mandatory filing fees, administrative fees, and expensive arbitrator hourly rates. Furthermore, arbitration is usually a confidential procedure, meaning that even if you win, your victory cannot be used as a helpful precedent for future lawsuits against that buyer or other buyers.

Additionally, compared to going to court, your procedural rights are often limited in arbitration. For example, your right to discovery (the process of asking an opposing party for information and documents critical to proving your case against them) is often extremely limited in arbitration. Moreover, if you agree to an arbitration clause, you are waiving any right to have your case heard before a jury of your peers. Finally, arbitration



generally does not allow for a class action approach to the resolution of a dispute with a buyer.



**If your contract offer includes an arbitration provision, you should try to delete it. It can be replaced with a provision stating that disputes will be resolved in the courts of your state.**

However, if you feel that you must accept a contract offer with an arbitration provision, it is important to make sure you have the answers to the following questions:

- Who may serve as the arbitrator in case of dispute?
- How will the arbitrator be selected?
- Where will the arbitration take place?
- Will the arbitration be binding (meaning that both you and the buyer must abide by the decision of the arbitrator)?
- Will you be allowed to appeal the arbitrator's decision if it is unfavorable to you? (Generally, arbitrator decisions cannot be appealed.)
- Will you be allowed through the arbitration process to obtain the documents or other evidence from the buyer that you need to prove your position in the dispute?
- Who will pay for the cost of the arbitration?
- If one side loses, will they have to cover the full cost of the arbitration?
- Will the loser also have to cover the other party's attorneys' fees and costs for the arbitration, or will each side cover their own costs?

All of these questions should be answered before you sign an organic contract with an arbitration provision.

**Contracts for Poultry and Swine Producers Must Include Arbitration Opt-Out Language**

Under the federal Packers and Stockyards Act, a livestock contract that requires the use of arbitration to resolve any controversy arising under it must contain a provision disclosing that a poultry or swine producer, prior to entering the contract, may opt out of the arbitration provision.

**Specialty Arbitration and Associated Rules**

Some organic contracts may require that arbitration be conducted by and under the rules of an organization dedicated to one type of commodity. These specialty arbitration organizations generally each have their own arbitration rules. For example, organic seed contracts might call for arbitration under the International Seed Testing Association (ITSA) rules, and organic grain contracts might call for National Grain and Feed Association arbitration rules to apply.

Although a specialty arbitration organization may offer the benefit that it is familiar with the market for a particular commodity, all of the downsides of general arbitration typically also apply in specialty arbitration, including potentially prohibitive expenses, required confidentiality, and limited procedural rights.

Regardless of which set of arbitration rules your contract calls for, if you are considering agreeing to binding arbitration, make sure to obtain and read a copy of the rules and procedures that will govern any disputes between you and the buyer. Or, consult an attorney who can help you understand the rules.

**Does your contract require mediation of disputes?**

Contracts might include a clause requiring the parties to attempt mediation or to make good faith attempts to settle disputes prior to filing a lawsuit or proceeding to arbitration. These clauses can be helpful to farmers because they can provide an opportunity for resolving a dispute outside of the more expensive court and arbitration processes. If your contract does not have a mediation clause, consider trying to include one.

Questions to Consider Regarding Mediation Include:

- Who may serve as the mediator?
- How will the mediator be selected?
- Where will the mediation take place?
- Who will pay for the cost of the mediation?
- Are the parties intending to exit mediation with a signed settlement agreement? (If there is no signed agreement between the parties, the agreement reached in mediation may be difficult to enforce; either party could decide not to follow the agreement at any time, and the other party would have difficulty proving that there was in fact an agreement.)
- What is the next step if the mediation is unsuccessful?
- Are the parties willing to participate in more than one mediation session?
- Must representatives of each party with settlement authority be present at the mediation?
- Must the mediation be conducted in person, or might the mediation be conducted via conference call?
- It is helpful for these questions to be answered in the text of the contract to help the mediation process run smoothly.

**Does the contract discuss who might have to pay attorney fees or costs?**

Contracts often include provisions stating that if there is a legal dispute related the contract, the party who loses the dispute will be required to pay the winner's legal fees and costs. This is called "fee-shifting," and can be dangerous for farmers because buyers may hire expensive lawyers to help ensure a win in court. In addition to attorney fees, costs can include court filing fees, copying fees, travel expenses, costs to hire expert witnesses, and more. These expenses can add up quickly, especially in a complicated contract dispute.

**Example: Fee-Shifting “Loser Pays”**

In any proceeding to enforce the terms of this agreement, the prevailing party shall be entitled to recover from the losing party its reasonable attorney fees and direct costs incurred by the prevailing party.



Since you cannot control how much money a buyer might spend in a legal battle, you may wish to agree that each side will pay their own legal fees—no matter who wins.

**Example: Better Attorney Fees and Costs Provision**

In the event of a dispute related to the contract, each side shall pay its own attorney fees and costs.



If the buyer will not agree to a provision requiring each party to pay their own legal fees, at minimum the contract should make clear that whoever loses must pay the other party's legal fees. It is not advisable to sign a contract in which only you are required to pay the buyer's legal fees, and not vice versa.

**Does the contract mention “liquidated damages” or other penalties?**

Liquidated damages are a predetermined amount of money that must be paid if a party fails to perform a contract promise. As a general rule, liquidated damages should not exceed the estimated value that the injured party would have received under the contract if the contract were fully performed.<sup>1</sup> If the liquidated damages are too high, a court might not enforce the provision, or might reduce the amount of damages.

Consider whether you want to sign a contract that would require you to pay a set amount of money to a buyer if you breach the contract. You might want to attempt to delete the provision, or you might attempt to

negotiate a lower amount. Alternatively, you might decide to negotiate a substitute for cash damages. For example, you might pledge a future crop to the buyer instead of cash because it might be easier for you to deliver a crop than cash.

In general, be cautious when signing a contract with a liquidated damages provision (or any cash penalties, for that matter).

## **CHAPTER 10 — ENDNOTE**

<sup>1</sup> U.C.C. § 2-718 (1977).



# 11

## Important Details

- [11-1](#) Does the contract prohibit assignment?
- [11-2](#) Does the contract have a “merger” or “entire agreement” provision?
- [11-3](#) Does the contract state that waiver of a contract promise does not constitute permanent waiver?
- [11-4](#) Does the contract have a “severability” provision?
- [11-5](#) Does the contract state that you and the buyer prepared the contract together?

### CHAPTER QUICK TIPS

#### **A Merger Provision Means You Can't Rely on Agreements Made Prior to Entering into the Contract Agreement**

If your contract has a merger provision, you cannot rely upon any oral or written agreements made before the contract was signed. Put another way, if you agree to a merger provision, you agree that the black and white terms of the contract are the only rules of the contract relationship – unless you and the buyer later agree in writing to change the rules.

#### **Prohibition of Assignment Means You Can't Transfer Your Obligations to Another Farmer**

Assignment involves transferring a party's duties and rights under the contract to another individual or business entity. If you are prohibited from assigning the contract, you cannot arrange for another organic farmer to fulfill your contract promises for you.





## IMPORTANT DETAILS

The types of provisions discussed in this chapter are common contract provisions (often referred to by non-lawyers as “standard” or “boilerplate” contract terms). These legal details can seem unimportant and removed from to the main purpose of the contract. However, if a problem or disagreement arises, and you end up in court or in another dispute resolution process, the provisions discussed below could have a very significant impact on the outcome.

### **Does the contract prohibit assignment?**

Assignment means transferring a party’s duties and rights under the contract to another individual or business entity. If you are prohibited from assigning the contract, you cannot arrange for another organic farmer to fulfill your contract promises for you.

Parties usually want to include a prohibition on assignment because:

- (1) they don’t want the disruption associated with a new, potentially unknown contract partner, and/or
- (2) they have a strong preference for working with the particular person or company performing the contract.



In the organic farming context, a buyer could be particularly interested in contracting specifically for your organically produced crop or livestock because the buyer knows and trusts your practices. Assigning the contract to another certified organic producer, even someone fully capable of delivering the contracted product, might leave the buyer uncertain whether they will get the same quality product that you would have supplied. Likewise, if a buyer you have built a relationship with assigns its contract rights to another company, you might not have the same level of confidence in the new buyer’s grading standards or payment practices.

### Prohibition on Assignment Could Cause Problems

A provision prohibiting assignment of your contract rights and obligations could be a problem if you are considering transferring ownership of your farm at any time during the life of the contract (which could be quite a long time, especially if the contract renews automatically). If so, you should think about negotiating language allowing assignment.

If you are worried that you may not be able to fulfill the contract for some other reason (such as serious illness or foreclosure), you may also want to negotiate assignment privileges. The negotiated language could allow assignment to specific individuals (such as your adult child or children) or to any other entity or individual without limit.

Sometimes, contracts include language prohibiting assignment unless the non-assigning party gives written permission. This is better than an all-out prohibition on assignment, but can still be somewhat risky because the party can always refuse permission.

### Assigning Payment

Assignment of contract rights can also involve assigning payment under the contract to a third party. For example, a farmer could assign payments under a contract to a lender or other creditor, such as an input supplier. To have more flexibility in obtaining operating credit, you may want to negotiate with the buyer to allow all or a portion of the payment owed to you to be paid directly to your creditor(s) through such an assignment.

### **Does the contract have a “merger” or “entire agreement” provision?**

A “merger” provision or “entire agreement” provision states that the written contract is a complete statement of the terms of the agreement that completely replaces (or “supersedes”) any prior or additional terms, representations, or agreements. The effect of this kind of provision is to formally state that your entire relationship is detailed by the written contract, and by the written contract alone. The merger provision means you cannot rely upon any papers that are not incorporated by the contract, and you cannot rely upon any oral conversations or emails. Put another way, if you agree to a merger provision, you agree that the black-and-white terms of the contract are the only rules of the contract relationship.



Example: Merger Provision

This Contract contains the entire agreement between the parties, with respect to the subject matter hereof, and supersedes and merges all prior negotiations, letters of intent, or understandings between the parties, whether written or oral. There are no conditions to this Contract that are not set forth herein.

Merger provisions are very common and most likely should not be a problem. This is particularly true because, even without a merger provision, you most likely may not rely on agreements outside of the written contract. As discussed earlier in this guide, it is always smart to put everything in writing, including anything the buyer says about the contract during negotiations, as well as any changes you make to the contract during the life of the contract. (See Chapter 1 for more detail.)

**Does the contract state that waiver of a contract promise does not constitute permanent waiver?**



Example: Single Waiver Does Not Mean Permanent Waiver

The failure of either party to require the performance of any provision hereof or the waiver by either party of any default hereunder will in no manner affect such party's right at any later time to enforce such provision.

If a party fails to meet some requirement in a contract and the other party does not object, the failure to object is considered a “waiver” of the requirement. For example, a landlord might accept late payment on a lease, or a buyer might accept a different quality, variety, or quantity of product than intended. Parties might waive a contract requirement for many reasons. For example, they might not consider the violation significant; they might be dependent on the ongoing contract relationship

and not want to risk termination; the other party might be having difficulty, and so they choose to be lenient; or they might have simply failed to notice the violation.

Because waiver of a violation means that the contract relationship will continue, a question can arise as to whether the “waived” requirement is still a requirement going forward. To address this question and preserve a party’s right to enforce all contract terms, even if the terms have been waived in the past, contracts often include a provision which states that a waiver or failure to enforce a requirement has no effect on the waiving party’s right to enforce the requirement in the future. Buyers who include a provision like this in organic contracts want to make sure that, if they are lenient about something early in the relationship, the farmer will still be bound by the contract requirements going forward.

For example, a contract might require you to make a delivery on the first of the month, and might also provide that the buyer can cancel immediately if you deliver after the third day of the month. Let’s say you consistently deliver on the fifth day of the month for six months. The buyer never complains. Then, in the seventh month, you deliver on the fifth day again. This time, the buyer cancels the contract, pointing to the provision allowing them to cancel if you deliver after the third day of the month. A “no waiver” provision in the contract would prevent you from arguing that, since the buyer allowed you to deliver on the fifth of each month for so long, the buyer can’t now say that the fifth of the month is a violation and cancel the contract. In fact, the “no waiver” provision allows the buyer to do exactly that—at one point treat a violation of the contract as unimportant, but later hold you to the exact language of the contract.

As the above example shows, a “no waiver” provision can be risky if you have become accustomed to a modified interpretation of the contract, and the buyer suddenly decides to enforce the exact requirements. Basically, what you need to remember is that even if a buyer has allowed you to stray from the terms of the contract in the past, you are always at risk if you stray in the same way in the future—especially if you have signed a contract that expressly states there will be no waiver of contract terms.

### **Does the contract have a “severability” provision?**

A severability provision generally states that if one part of the contract is found to be invalid or unenforceable (usually by a judge), the rest of the contract would remain in effect. Sometimes these provisions also include language stating that the parties agree to make reasonable efforts to substitute a valid provision that implements the basic intent of the provision that was held to be invalid.

This type of provision helps prevent a whole contract from being ruled invalid when the problem can be limited to a single provision or provisions. By explicitly stating that the different parts of the contract are independent of each other and can be separated as needed, the intent of the severability clause is to maintain as much of the original contract language as possible.

As long as you understand how severability works, it is unlikely that this type of provision will cause a problem for most farmers.



**Example: Severability Provision**

Severability: All provisions of this Agreement, and all portions of such provisions, are intended to be, and shall be, independent and severable. If a court finds any provision of this Agreement invalid or unenforceable, the remainder of this Agreement shall be interpreted so as best to effect the intent of the parties.

**Does the contract state that you and the buyer prepared the contract together?**

It is a basic rule of contract interpretation that if it is not clear what a particular provision means, and each party would benefit from a different possible meaning, the meaning that benefits the party who did not write the contract should be used. This is called “interpreting against the drafter.” The reasoning is that the person who wrote the contract had the opportunity to use the words they wanted and say exactly what they intended to say; if the drafter had wanted their interpretation of the unclear language to have effect, they should have written it clearly.

To get around this rule of contract interpretation, many commercial contracts include a provision stating the contract was mutually prepared. By signing a contract with such a provision, non-drafting parties agree that they are equally responsible for all of the contract language and give up the claim to have any unclear provision interpreted in their favor.

If you and a buyer truly prepare a contract together through a series of negotiations, that is fantastic. If that is the case, this type of provision is accurate and will not pose a problem. If, however, as is more common, you were handed a pre-printed contract drawn up by the buyer alone,

you might be a little concerned about signing a contract that says you prepared it together.

**Example: Mutual Preparation of Contract Provision**

Buyer and Seller agree this agreement was prepared mutually by both parties; no uncertainty or ambiguity shall be construed against either party.



You might think about whether you would like to maintain the slight advantage over the buyer that you might have in court if a dispute arises and the contract does not include a mutual preparation provision. However, the presence or absence of such a provision would probably not have a significant effect on the outcome of a dispute. In many circumstances, the slight advantage of not having such a provision would likely not make much difference. Furthermore, even if the contract does have a mutual preparation provision, the judge might still inquire about the actual circumstances of the contract preparation and take that into account when interpreting unclear provisions.

Thus, although it may be more advantageous to sign a contract without a mutual preparation provision, this kind of provision is unlikely to create significant risk.

# 12

## Problem Solving

- [12-1](#) Resolving Contract Disputes
- [12-3](#) Enforcing an Organic Contract Against the Buyer
- [12-10](#) Laws Governing Contract Disputes
- [12-16](#) Ten Common Organic Contract Problems
- [12-18](#) Buyer Breaches
- [12-25](#) Organic Farmer Breaches

### CHAPTER QUICK TIPS

#### **Hiring An Attorney**

In a best case scenario, your attorney will: (1) be an experienced contract lawyer; (2) regularly represent farmers; and (3) be familiar with the NOP regulations. At the very least, however, your attorney should either have contract law experience or regularly represent farmers. If your attorney is not responsive to your needs, frequently fails to return calls, or makes you feel uncomfortable, find a different attorney. You can fire an attorney at any time.

#### **Small Claims Court Can Help Farmers**

If the amount of money involved in a contract dispute is relatively small (several thousand to \$10,000+, depending on the state), you may be able to take advantage of state “conciliation courts” or “small-claims courts,” which resolve issues faster and more informally.





## RESOLVING CONTRACT DISPUTES

During the period that the organic contract is in effect, disputes may arise between you and the buyer. If a problem does occur, it is helpful for you to understand your basic legal rights and obligations—even if you never set foot in a courtroom. You have more leverage in negotiating a solution when you can demonstrate to the buyer that you understand your legal rights. Similarly, if you understand your legal obligations, you can make an educated decision about which side has the stronger argument, and whether it would be worth the time, energy, and money it would take to pursue your claims against the buyer.

This chapter discusses some common problems that occur during the course of organic contract performance and provides an overview of the legal principles and arguments frequently used in these situations.

### **IMPORTANT NOTE:**

This guide can provide only a brief overview of the legal landscape related to organic contract disputes. If you encounter a contract problem, the best course of action is to consult an attorney licensed to practice in your state. An attorney can identify the applicable laws for the facts of your particular dispute.

See page 12–4 of this chapter for tips on hiring an attorney.

## **Determining Your Contract Rights and Obligations**

At the outset, it is important to understand that your contract rights and obligations are determined by three main sources, listed in order of importance:

1. The contract
2. Federal contract law
3. State contract law

This means that, in addition to the actual words of the contract, you may have other rights and obligations created by federal and state law. It also means that while the contract language will control the majority of any dispute, it is possible that some contract provisions might be illegal, unenforceable, or superseded by state or federal law. For example, if you are a farmer in Minnesota and you signed a contract with a confidentiality provision prohibiting you from sharing the contract language with anyone, Minnesota state law most likely nullifies that provision.<sup>1</sup>

A detailed discussion of each state's contract laws is beyond the scope of this guide. Each state's laws are unique. Therefore, if you have a contract dispute, it is always best to consult an attorney licensed to practice law in your state—preferably one who is familiar with agricultural contracts and the National Organic Program (NOP) regulations.

### **A Note on the NOP Regulations**



Organic farmers should always be mindful of how any contract dispute (and any potential agreements to settle a dispute) could conflict with the NOP regulations. Do not agree to resolve a dispute in a manner that would cause you to violate your Organic System Plan (OSP) and potentially lose organic certification.

## **ENFORCING AN ORGANIC CONTRACT AGAINST THE BUYER**

### **Farmers Have Options If the Buyer Refuses to Fulfill Contract Promises**

#### First Steps When Problems Arise

Each farmer has his or her own comfort level with confrontation, and it is well known that contract disputes can damage valuable farmer-buyer relationships. Ideally, farmers and buyers will be able to resolve disputes informally outside of court.

If a dispute is brewing, send a letter, call the buyer, or set up a face-to-face meeting with the buyer. Try to come up with a workable solution to the problem. If you and the buyer do resolve the problem, be sure to record any agreement in writing. Still, in case you and the buyer cannot reach an agreement, keep records of the communications you have regarding the problem; they could become important in any later lawsuit.

If legal action is something you would consider, be careful not to let too much time pass between the dispute and filing a lawsuit. A consultation with an attorney can help to determine how to best preserve your legal rights if you decide to go to court (or if the buyer sues you).

Sometimes farmer-buyer disputes simply cannot be resolved without a lawyer or a formal dispute resolution process, such as mediation or litigation. The remainder of this section discusses some of the actions farmers can take to enforce their contracts against buyers who fail to keep contract promises.

#### Consult an Attorney

In the case of a contract dispute, you should consult an attorney for help. Attorneys can help you understand your legal position, and can help you understand the pros and cons of various options for resolving the dispute.

**Tips for Finding an Attorney**

- Look for an attorney licensed in your state who regularly practices contract law. Ask whether the attorney regularly does contract litigation (representing people in court cases about contract disputes). Additionally, ask whether the attorney can help you settle the case outside of court (by negotiating a settlement agreement, for example).
- Look for an attorney who is also familiar with agriculture—someone who frequently represents farmers.
- In a best-case scenario, your attorney will: (1) be an experienced contract lawyer; (2) regularly represent farmers; and (3) be familiar with the NOP regulations. At the very least, however, your attorney should either have contract law experience or regularly represent farmers.
- Hire an attorney you feel comfortable with, and do not hesitate to shop around to find the best fit and value. An experienced contract attorney familiar with agriculture will likely spend fewer hours on your case (and thus, cost less) than an attorney without contract or agriculture experience.
- You can also ask about negotiating a flat rate for the attorney's services instead of paying an hourly rate. Flat fees can lower the cost of both experienced and less-experienced attorneys.
- If your attorney is not responsive to your needs, frequently fails to return calls, or makes you feel uncomfortable, find a different attorney. You can fire an attorney at any time.
- If you are looking for attorney referrals, contact FLAG or your state or local bar association. FLAG maintains a database of attorneys who have expressed interest in representing family farmers. You can reach FLAG by phone at 651-223-5400, or by email at [lawyers@flaginc.org](mailto:lawyers@flaginc.org). Minnesota farmers can call FLAG's toll-free line (877-860-4349).



### Try Mediating the Dispute

If you or your attorney have communicated with the buyer but have been unable to resolve your contract issues, mediation can be a useful process. Many communities offer free or affordable dispute resolution services. You can mediate on your own or with the help of an attorney.

Note, however, that mediation is typically non-binding. This means that you and the buyer could reach a mediated agreement on Monday, and either party could decide to back out on Tuesday without any legal consequences. Unless both sides sign a written settlement agreement, the buyer cannot be compelled to abide by the mediated outcome.

Furthermore, you cannot force an unwilling buyer to mediate (unless the contract states that the buyer must mediate contract disputes).

### File a Lawsuit Against the Buyer

If mediation fails, your next option is likely a lawsuit. Still, it is important to recognize that lawsuits can take years to resolve, can involve expensive court costs and attorney fees, and can be extremely draining in terms of physical and emotional energy.

Lawsuits can take many different routes. In the best-case scenario, simply filing a lawsuit will make the buyer more interested in working out a settlement.

On the other hand, filing a lawsuit might irritate or anger the buyer, and could make settling the dispute impossible. With a view toward protecting itself from future lawsuits, a buyer might choose to adopt a “fight-to-the-death” litigation strategy in the hopes of making you an example of what happens to farmers who sue. In this kind of situation, lawsuits can take many years and cost many tens of thousands of dollars.

- *Arbitration*

It is very important before filing any lawsuit related to a contract dispute to determine whether the contract requires you to resolve contract disputes through arbitration. Arbitration is a private decision-making process in which a private individual (an arbitrator) decides a dispute after hearing from both sides.

**Arbitration Does Not Favor Farmers**

If you signed a contract with an arbitration clause, you have likely waived your right to use the public court system to settle your dispute. This is an undesirable position, because arbitration procedures generally heavily favor larger companies, such as most buyers—not farmers. Perhaps most problematic, arbitration is often prohibitively expensive for individual organic farmers.

If you are in a contract dispute and have a contract with an arbitration provision, consult an attorney familiar with arbitration proceedings who is licensed to practice law in your state. An attorney can help you decide whether to proceed with arbitration, settle with the buyer, or take another course of action. In rare situations, arbitration clauses and arbitrators' decisions can be successfully challenged in court.

See Chapter 10, pages 10–4 through 10–6, for a more detailed discussion of arbitration.



If the contract does include an arbitration agreement, you will likely be required to arbitrate your dispute outside of court. If the contract does not require arbitration, you are generally free to file a lawsuit against a buyer to resolve any contract-based dispute.

See Chapter 10, pages 10–4 through 10–6, for a more detailed discussion of arbitration.

- *Small-Claims Court*

If the amount of money involved in your dispute is relatively small (several thousand dollars to \$10,000+, depending on the state), you may be able to take advantage of a streamlined and less costly court process. Most states have “conciliation courts” or “small-claims courts” which resolve issues more informally and within shorter time frames. Be aware, though, that each state has its own rules about how much money is a “small claim,” as well as what kinds of cases can be heard in small-claims court. Check with your local state court administrator to find out whether your dispute could be handled in small-claims court.

- *Class Action Lawsuits*

Farmers sometimes consider filing class-action lawsuits against certain larger buyers for widespread and ongoing problems. When considering class actions, it is important to know that these lawsuits often take far longer than individual lawsuits; they can take up to a decade or more. Class action lawsuits are very complicated, are extremely expensive, and will not solve anyone's immediate problems. Still, class actions can be useful to help address systemic, long-term problems. In addition, lawyers who litigate class actions will often work on a contingency basis, meaning that they do not get paid unless their clients are successful.

- *There Are Risks: Discovery and Counterclaims*

Filing a lawsuit will mean that both you and the buyer will go through a process called “discovery.” In the discovery phase of a lawsuit, while you will have the opportunity to obtain information about the buyer and its actions, the buyer will have the opportunity to obtain information about you, your family, and your farm. During discovery, parties will often seek information an ordinary person would consider private. The buyer's attorneys might try to find information about you—even if it is unrelated to the dispute—that could place you in an unflattering light or reveal other difficulties you've been having. Much of this information could be made public, since court filings are usually public record.

Additionally, filing a lawsuit against the buyer gives the buyer a convenient setting to file claims against you. These are called “counterclaims” and can be any claims related to the contract. For example, if you are suing the buyer on a price issue, the buyer could turn around and file counterclaims against you for violating other parts of the contract, such as product quality, delivery time, or management practices. These might be issues that the buyer would never have bothered with otherwise, but your lawsuit might give it the opportunity and perhaps the incentive to throw as much at you as it can. Also, if the buyer does file counterclaims, it becomes harder for you to withdraw your lawsuit if you later decide, for example, that it is costing too much or the discovery requests are too burdensome. If the buyer files counterclaims, the lawsuit cannot be dismissed until all of the claims—yours and the buyer's—have either been withdrawn or ruled upon by the judge.

**Weigh Pros and Cons of Litigation**

Farmers should carefully weigh pros and cons before deciding to file a lawsuit against a buyer. There is little downside, however, to learning as much as you can about your options. Educating yourself about contract law or consulting an attorney about your problem is not the same thing as deciding to file a lawsuit. An attorney licensed to practice in your state can help you understand your options and perhaps even resolve your dispute out of court—by giving you behind-the-scenes advice, explaining the laws that apply to your situation, and/or helping you communicate with the buyer.

**Lawsuits Will Only Take You So Far**

Aggrieved farmers wanting revenge against a buyer are not likely to find what they are looking for in a courtroom. In contract disputes, judges generally try to reach a result that leaves each party in the position they would have been in if the contract had been fully performed by both parties. And, even successful parties must generally subtract from any damages award the time and money spent on the lawsuit. In some instances, farmers may be able to recover attorney fees and court costs from buyers as part of a court award, but this “fee-shifting” usually occurs only when the contract explicitly requires the losing side to pay the other side’s fees. Of course, contracts can (and often do) require farmers who lose in court to pay buyers’ attorney fees and court costs.

Also, in a contract lawsuit, you will not be able to use evidence outside the contract language itself to prove that the contract means something other than what it says in black and white. The prohibition of outside evidence is called the “parol evidence rule.” This means you should not count on evidence outside of the contract when analyzing your likelihood of success in court. The court will not consider whether the buyer reneged on oral promises, whether the buyer acted like a jerk, whether your family has encountered tough times, or whether your organic farm is a benefit to society. When you are thinking about your likelihood of success in court, try to take issues like these out of the equation.

**If a Buyer Sues You...**

Finally, if a buyer decides to take legal action against you, consult with an attorney licensed to practice law in your state as soon as possible.



Lawsuits are very difficult for non-lawyers to successfully handle by themselves. In particular, when you are sued, you are required to file very specific legal papers with the court by certain deadlines. If you miss these deadlines, you can lose important rights. For example, failing to respond to a legal complaint can lead to a default court judgment against you (that is, an order saying the buyer wins) that can be difficult or impossible to overturn. Consequently, if you receive notice that a buyer has filed a legal complaint against you, contact a lawyer immediately.



### **Practical Tips If You Are Sued**

- Take the lawsuit seriously. Judges are generally unsympathetic to people who fail to respond to legal notices or fail to show up at required court appearances without a very, very good excuse (such as being hospitalized for a serious illness). So, even if you cannot afford to hire an attorney, make sure to respond to court notices and to attend scheduled court appearances.
- You can always call the court and talk to court employees about court procedures and scheduling court dates. Failing to communicate with the court—either on your own or through your attorney—is usually the worst course of action in a civil lawsuit. You can also write letters to the judge assigned to your case. Be respectful in all communications.
- If you are scheduled to appear in court but you cannot make the hearing, make sure to contact the court as soon as possible (preferably at least 24 hours before your scheduled appearance).
- Make a serious effort to comply with every aspect of any order the judge issues—whether oral or written. If you do not comply, the judge could hold you in contempt and possibly even put you in jail.
- You have a much better chance of success in court if you have attorney representation.

## LAWS GOVERNING CONTRACT DISPUTES

If a party fails to keep a contract promise, that party has “breached” the contract. When a party breaches a contract, the law may provide a remedy to compensate the other party.

### **Determining Farmers' Legal Rights and Obligations After Breach of Contract**

To determine your legal rights and obligations after a breach, first look to the language of the contract. What does it say about your particular situation? If the contract doesn't say anything about your situation, you must look to federal and state contract law for guidance. As mentioned earlier, in a few situations, federal or state law might even nullify parts of the contract.

### **Federal Laws Relevant to Organic Contracts**

Although the majority of contract law is controlled by each individual state, the federal government has enacted a few laws relevant to organic contracts. The most significant federal contract laws apply only to farmers producing certain commodities.

#### **Perishable Agricultural Commodities Act (PACA) for Produce Farmers**

The Perishable Agricultural Commodities Act (known as PACA)<sup>2</sup> covers only the produce industry. PACA, which was designed to ensure fair business dealings in the produce industry, created: (1) an administrative process for farmers seeking full payment under fruit and vegetable sales contracts; and (2) a trust mechanism to provide some payment for farmers if a buyer is bankrupt. Farmers who sell perishable commodities can file PACA complaints against buyers who fail to pay promptly and fully.

- *PACA Money Damages Complaint*

If a buyer fails to pay promptly and fully, you may be able to recover unpaid amounts (plus any losses caused by the buyer's failure to pay fully and promptly) by filing a PACA complaint. Produce buyers are required to pay the full contract price within the time frames PACA establishes (typically 5 – 20 days), unless the contract states a different payment deadline.<sup>3</sup> You can file a

PACA complaint even if the buyer paid you part of the contract price.<sup>4</sup>

You can also file a PACA complaint to recover losses caused by a buyer who wrongfully destroys or “dumps” your produce without reasonable cause or proper documentation.

You must file a PACA complaint for money damages with the U.S. Department of Agriculture’s (USDA) PACA branch within nine months of the failure to make full and prompt payment or within nine months of a wrongful rejection of a farmer’s delivery.<sup>5</sup>

See the PACA website at <http://www.ams.usda.gov/AMSV1.0/PACA> and click on the links under “Dispute Resolution” for more information.

- *PACA Non-Monetary Disciplinary Complaint*

You may file a PACA disciplinary complaint (non-monetary) against a buyer who fails to pay promptly and fully within two years of failure to make full and prompt payment or within two years of a wrongful rejection.<sup>6</sup>

See the PACA website at <http://www.ams.usda.gov/AMSV1.0/PACA> and click on the link under “Reporting Unfair Trade Practices” for more information.

See the PACA website for additional details and to download complaint forms: <http://www.ams.usda.gov/AMSV1.0/PACA>.

### Packers and Stockyards Act (PSA) for Livestock and Poultry Producers

The Packers and Stockyards Act (PSA)<sup>7</sup> applies solely to the livestock (cattle, swine, lamb, and goats) and poultry industries.<sup>8</sup> The goal of the PSA is to promote fair competition and ensure fair trade practices in livestock and poultry markets. To that end, it prohibits livestock packers and poultry processing companies<sup>9</sup> from engaging in any unfair, unjustly discriminatory, deceptive, price manipulative, or trade-restraining practices.<sup>10</sup> In recent years, several federal courts have issued decisions that make it hard for livestock and poultry producers to succeed in lawsuits alleging that packers or processors have engaged in these prohibited practices.<sup>11</sup> If you are considering filing such a lawsuit, you should consult with an attorney familiar with these PSA enforcement issues.

- *PSA Trust*

In addition to the general prohibition against certain unfair practices, the PSA and the rules implementing it, administered by

USDA's Grain Inspection and Packers and Stockyards Administration (GIPSA), also regulate specific aspects of the relationship between (1) livestock and poultry producers,<sup>12</sup> and (2) the packers and processors with which they do business.

One important aspect of the PSA rules is the establishment of a trust to ensure that livestock and poultry producers are fully paid for their products.<sup>13</sup> In order to collect payment through the PSA trust, producers must satisfy detailed written notice and complaint procedures and meet tight deadlines. If you have sold livestock or poultry to a packer or processor, or have raised swine or poultry under a production contract growing arrangement, and have not received timely or full payment, you should immediately determine whether you can obtain payment through the PSA trust.

You can obtain more information about the PSA trust at <http://www.gipsa.usda.gov/psp/livetrust.html> (livestock) or <http://www.gipsa.usda.gov/psp/poultry.html> (poultry), or by contacting USDA's Packers and Stockyards Administration office in your state or in Washington, D.C.

#### Agricultural Fair Practices Act (AFPA) for Farmers in Associations

The Agricultural Fair Practices Act (AFPA)<sup>14</sup> provides certain contract protections for farmers who have joined or wish to join a farmers' association. The AFPA is designed to protect the rights of farmers to associate in cooperative organizations. It prohibits buyers from taking certain retaliatory actions against farmers because of the decision to join (or not to join) a farmers' association. One section of the law prohibits buyers from discriminating against any farmer with respect to price, quantity, quality, or other terms of purchase because of the farmer's membership in an association. This law could protect you if you can prove that a buyer discriminated against you because of your membership in a farmers' association. However, the burden of proving discrimination is on the farmer, and it can often be difficult to prove a discriminatory motivation for a buyer's decision.

Some farm policy groups working on behalf of organic family farmers have advocated making the AFPA stronger by changing the law to close loopholes and make it easier for farmers to bring a claim.<sup>15</sup> Advocates are also calling for more robust enforcement against buyers who violate the law.<sup>16</sup>

## **State Laws Relevant to Organic Contracts**

### **Article 2 of the Uniform Commercial Code**

The Uniform Commercial Code, commonly referred to as the “U.C.C.,” is a comprehensive set of rules for commercial transactions that has been adopted, with small but sometimes significant variations, in all 50 states. The U.C.C. is made up of several sections, called “Articles.” Article 2 of the U.C.C. applies to contracts for the sale of goods worth more than \$500. Because organic commodities are “goods” under the U.C.C., Article 2 of the U.C.C. applies to organic contracts.



### **State Versions of the Uniform Commercial Code**

When states adopt U.C.C. provisions, they often use numbering schemes similar to U.C.C. numbering. Therefore, if you are looking up your state’s version of a U.C.C. section, it may be helpful to look for similar numbering within the state statute. For example, state law versions of U.C.C. § 2-703 (Seller’s Remedies in General) include:

California – Cal. Commercial Code § 2703

Florida – Fla. Uniform Commercial Code § 672.703

Minnesota – Minn. Stat. § 336.2-703

Nebraska – Neb. Uniform Commercial Code § 2-703

New Mexico – N.M. Stat. § 55-2-703

Wisconsin – Wis. Stat. § 402.703

With the exception of Louisiana, every state has adopted a version of U.C.C. Article 2. Although each state’s version of Article 2 is slightly different, the major themes are generally consistent. Pages 12–16 through 12–28 of this chapter will highlight some of the important concepts of Article 2 that come into play when buyers and farmers breach contracts.

### **State Laws Specific to Agricultural Contracts**

In addition to adopting U.C.C. Article 2 provisions that regulate contracts generally, several states have enacted laws specifically regulating agricultural contracts. In general, these laws are designed to ensure some level of fairness in agricultural contracting. Although a detailed

explanation of these laws is beyond the scope of this guide, some of the state laws that might apply to organic farmers are discussed below.<sup>17</sup>

Some states have enacted laws applicable only to certain agricultural sectors and certain types of contracts. For example, some states have enacted laws related to production contracts for livestock and poultry. These laws have goals similar to the goals of the federal Packers and Stockyards Act—eliminating unfair practices in the livestock and poultry industries.

Arkansas has enacted fair-dealing legislation applicable only to livestock production contracts and poultry production contracts.<sup>18</sup> Similarly, Georgia has enacted legislation providing protection only for poultry production contracts,<sup>19</sup> and Kansas has separate laws regulating swine production contracts and poultry production contracts.<sup>20</sup> If you are an organic farmer raising livestock or poultry under a production contract in Arkansas, Georgia, or Kansas, be sure to check whether these laws apply to your contract.

Other states have enacted laws granting broad contract protections for multiple agricultural sectors, including producers of livestock, milk, and field crops. Illinois,<sup>21</sup> Iowa,<sup>22</sup> Minnesota,<sup>23</sup> and Wisconsin<sup>24</sup> have each enacted broad legislation with strong protections against unfair trade practices. Some of these protections include prohibitions against stringent confidentiality provisions, requirements that disputes be resolved in the courts of the state where the farmer is located, allowances for the farmer to cancel the contract within a certain time after signing, and specific disclosure requirements.

In addition, California has enacted an agricultural lien law that creates a lien for farmers which attaches upon delivery of the contracted product and protects farmers when buyers fail to make payment.<sup>25</sup>

Finally, Minnesota has enacted a Wholesale Producer Dealers Act similar to the federal Perishable Agricultural Commodities Act (PACA), protecting Minnesota farmers who sell fruits, vegetables, and other perishables against buyers who do not pay promptly and fully.<sup>26</sup>



**The law of the state where you live or farm may not govern your contract.**

Choice-of-law provisions are contract provisions that specify which state's laws will govern disputes related to the contract. The contract could state, for example, that your contract will be interpreted according to the laws of Delaware—even if you live in Wyoming. These provisions are often enforceable unless you farm in a state that prohibits choice-of-law provisions for agricultural contracts. See Chapter 10, pages 10–2 and 10–3, for further discussion of choice-of-law clauses.

**Additional State Law Protections**

There may be other state laws that affect your contract relationship even though they do not directly regulate agricultural contracts. For example, almost every state has laws generally prohibiting unfair and deceptive trade practices. These laws may also be applicable to organic contract disputes.

Again, if you are involved in a contract dispute, consult an attorney licensed to practice law in your state who is experienced with contract law.

## TEN COMMON ORGANIC CONTRACT PROBLEMS

Some of most common contract breaches occur when **buyers:**

1. Reject delivery
2. Fail to pay
3. Try to terminate the contract (before delivery and payment)
4. Fail to perform other contract promises
5. Declare bankruptcy

On the other hand, breach can also occur when **organic farmers:**

6. Fail to make delivery
7. Fail to deliver goods that meet quality standards
8. Try to terminate the contract (before delivery)
9. Fail to perform other contract promises
10. Declare bankruptcy

For each of the ten common contract problems listed in the box above, this section will discuss legal principles that are potentially applicable. Many of these principles are derived from Article 2 of the U.C.C. (discussed on page 12–13 of this chapter). Your state's version of the U.C.C. may be the same, slightly different, or completely different. The guide will also highlight other potentially relevant federal laws.

The purpose of this section is to make you aware of the range of legal remedies that may be available to farmers and buyers when a common contract dispute arises. You cannot assume that these principles will apply to your situation. First, the terms of the contract will often control the outcome of a contract dispute. Many of the legal principles discussed in this section are “fallback” principles, meaning that they apply only if



the contract is silent on a particular topic.<sup>27</sup> Second, applicable state laws (which may differ from the laws discussed here) will likely have a big impact on the meaning of your contract and the outcome of your dispute. Finally, this section does not cover the entirety of contract law; many other details and specialized rules must be taken into account.

As a result, if you are involved in a contract dispute, you should consult an attorney licensed to practice law in your state. This overview cannot substitute for an experienced lawyer who is familiar with the latest changes in federal and state laws and regulations. See page 12–4 of this chapter for tips on hiring an attorney.

## BUYER BREACHES

### Wrongful Rejection

If the buyer wrongfully rejects delivery of your product, first look to see what the contract says about the situation. If it says nothing, or is unclear, you may be able to:

- Withhold or stop any additional deliveries.<sup>28</sup>
- Cancel the contract.<sup>29</sup>
- Sell your products to another buyer.<sup>30</sup>
- Sue the buyer for money damages. Damages could be measured in three different ways:
  - (1) The difference between the contract price and the actual price you receive for the product from a new buyer, plus incidental damages (defined below), minus any savings you realize, if any, as a result of the breach.<sup>31</sup>
  - (2) The difference between the contract price and the organic market price, plus incidental damages, minus any savings.<sup>32</sup>
  - (3) If damages based on the actual price you received or the organic market price are inadequate to compensate you for the breach, damages could be based on your lost profits, plus incidental damages, minus any savings.<sup>33</sup>

Incidental damages include your commercially reasonable expenses in connection with: (1) stopping delivery; (2) transporting, storing, or caring for the products after the buyer's breach; (3) reselling the products; or (4) other issues resulting from the buyer's breach.<sup>34</sup>

If you sell fruit, vegetables, or other produce, and the buyer rejects your produce delivery without reasonable cause, you may be able to recover the contract price and any losses caused by the wrongful rejection by filing an administrative complaint under the federal Perishable Agricultural Commodities Act (PACA). See the earlier discussion on PACA (pages 12–10 and 12–11 of this chapter) for more information on PACA complaints.

If you raise and/or sell livestock, swine, or poultry, a wrongful rejection could give you a claim against the buyer under the federal Packers and Stockyards Act (PSA). As discussed earlier, the PSA prohibits buyers from

engaging in unfair, unjustly discriminatory, or deceptive trade practices.<sup>35</sup> However, to succeed on a PSA claim, you will likely have to prove in court that the buyer's practices adversely affect competition.

### **Failure to Pay in Full**

If the buyer fails to pay in full for your deliveries, first look to see what the contract says about such a situation. If it says nothing, or is unclear, you may be able to:

- Withhold or stop deliveries.<sup>36</sup>
- Cancel the contract.<sup>37</sup>
- Sell your products to another buyer (this likely works only if you still have the products in your possession).<sup>38</sup>
- Sue the buyer for damages. Damages could be measured in two ways, based on whether you can sell the products to another buyer:
  - (1) The difference between the contract price and the actual price you receive for the product from a new buyer, plus incidental damages (defined on the previous page), minus any savings you realize as a result of the breach.<sup>39</sup>
  - (2) If you can't sell the products to another buyer, the contract price of the accepted goods, plus incidental damages, minus any savings (such as avoiding shipping costs if you did not deliver the product).<sup>40</sup>

In some states, you may have the right to a state law agricultural lien against the buyer for the full contract price.<sup>41</sup> This type of lien grants the farmer a security interest in the commodity delivered to the buyer or the proceeds from the sale of the commodity. However, even if the applicable state law creates such a lien, the lien may or may not give you priority over the buyer's other creditors. Consult an attorney licensed in your state for advice about this type of lien.

If you sell fruit, vegetables, or other produce, and the buyer accepts the produce but fails to pay you fully and promptly, you may be able to recover the unpaid amounts (plus any losses caused by the buyer's failure to pay fully and promptly) by filing a PACA complaint. See pages 12–10 and 12–11 of this chapter for more information on PACA complaints.

If you raise and/or sell livestock, swine, or poultry, and the buyer fails to make full and prompt payment, you can initiate the PSA trust process by providing written notice to the packer or processor and USDA's Grain

Inspection, Packers and Stockyards Administration (GIPSA) within 30 days of the final date for the buyer to make prompt payment, or within 15 business days of being notified that a promptly presented payment check was dishonored.<sup>42</sup>

If the buyer continues not to pay after receiving this written notice, you may need to file a complaint in court to obtain an order directing the packer or processor to pay you. The court can order a packer whose average annual purchases of livestock exceed \$500,000 and a poultry processor whose average annual sales, purchases, or value of poultry raised under a growing arrangement exceeds \$100,000 to hold specified property in trust for your benefit as an unpaid cash seller or poultry producer. You can then get paid from this trust without competing with the buyer's other creditors.

You can obtain more information about making a claim against the PSA trust at <http://www.gipsa.usda.gov/psp/livetrust.html> (livestock) or <http://www.gipsa.usda.gov/psp/poultry.html> (poultry), or by contacting the GIPSA office in your state or in Washington, D.C.

### **Buyer's Repudiation**

When a buyer tells you it doesn't intend to perform its contract promises before you have made a delivery or received payment, this is considered "repudiation" of the contract. Repudiation can occur for all or a portion of the organic farm products under contract. If this happens to you, first look to see whether the contract addresses repudiation. If it does not, or is unclear, you may be able to:

- Withhold or stop deliveries.<sup>43</sup>
- Cancel the contract.<sup>44</sup>
- Sell your products to another buyer.<sup>45</sup>
- Sue the buyer for damages. Damages could be measured in three different ways:
  - (1) The difference between the contract price and the actual price you receive for the product from a new buyer, plus incidental damages (defined on page 12–18 of this chapter), minus any savings you realize as a result of the breach.<sup>46</sup>
  - (2) The difference between the contract price and the organic market price, plus incidental damages, minus any savings.<sup>47</sup>
  - (3) If damages based on the actual price you received or the organic market price are inadequate to compensate you for

the breach, damages could be based on your lost profits, plus incidental damages, minus any savings.<sup>48</sup>

If you sell fruit, vegetables, or other produce, and the buyer repudiates the contract before delivery, you may be able to recover the unpaid amounts by filing a PACA complaint. However, be aware that you must still make all reasonable attempts to try to sell your produce to another buyer (even for a lower price). You must file a PACA complaint for money damages with the USDA's PACA branch within nine months of the repudiation.<sup>49</sup> See pages 12–10 and 12–11 of this chapter for more information on PACA complaints.

If you raise and/or sell livestock, swine, or poultry, and the buyer repudiates the contract, you could have a claim against the buyer under the PSA if you could prove that the repudiation amounted to an unfair, unjustly discriminatory, deceptive, price manipulative, or trade-restraining practice.<sup>50</sup> In recent years, several federal courts have issued decisions that make it hard for livestock and poultry producers to succeed in lawsuits alleging that packers or processors have engaged in these prohibited practices. If you are considering filing such a lawsuit, you should consult an attorney familiar with PSA enforcement issues.

### **Buyer's Failure to Perform Other Contract Promises**

If the buyer fails to perform any other contract promise, first look to see what the contract says about the situation. If it says nothing, or is unclear, you may be able to:

- Sue the buyer for money damages, if you have been financially harmed.<sup>51</sup>
- Make a claim under the applicable state's unfair and deceptive trade practices law.

If you sell fruit, vegetables, or other produce, you could file a PACA disciplinary complaint (non-monetary) against the buyer within two years of the breach, but you would not recover any money damages from a disciplinary complaint.<sup>52</sup> Instead, you can request that USDA take disciplinary action against a buyer, including assessing fines, issuing warning letters, or suspending/revoking a buyer's PACA license. See pages 12–10 and 12–11 of this chapter for more information on PACA complaints.

If you raise and/or sell livestock, swine, or poultry, you could have a claim against the buyer under the PSA if you could prove that the failure to perform under the contract amounted to an unfair, unjustly discriminatory, deceptive, price manipulative, or trade-restraining

practice.<sup>53</sup> As discussed above, recent court decisions have made such claims much more difficult. If you are considering filing such a lawsuit, you should consult with an attorney familiar with these PSA enforcement issues.

## **Buyer Goes Out of Business or Is in Bankruptcy**

### **Buyer Goes Out of Business**

If the buyer goes out of business, the terms of your contract and state law will control what happens to your contract relationship. Thus, if the buyer goes out of business, or otherwise becomes insolvent, be sure to check what the contract says about the situation. The buyer's insolvency may also trigger certain state law-related outcomes; for example, you may be able to:

- Withhold or stop deliveries, unless the buyer will pay with cash.<sup>54</sup>
- Reclaim delivered products if the buyer has received the products on credit while insolvent. To reclaim, you must demand reclamation within 10 days after the buyer received the goods. Also, if you reclaim the products, you cannot sue the buyer for damages related to those products.<sup>55</sup>

The sections above on buyer's failure to pay in full and buyer's failure to keep other contract promises may also apply in situations when the buyer goes out of business.

You may also have the right to a state law agricultural lien against a buyer in bankruptcy for the contract price for delivered products. Consult an attorney licensed in your state for advice about state agricultural liens.

### **Buyer in Bankruptcy**

If the buyer enters bankruptcy proceedings, the federal Bankruptcy Code will control what happens to your contract relationship—with some reference to state law and the terms of your contract. Bankruptcy rules are complex and can often override the language of a contract. It is always recommended to consult a bankruptcy attorney if you are dealing with a buyer in bankruptcy.

You may also have the right to a state law agricultural lien against a buyer in bankruptcy for the contract price for delivered products. However, a state law lien may or may not have priority over the buyer's other creditors. Consult an attorney licensed in your state for advice about state agricultural liens.

If you sell fruit, vegetables, or other produce, and comply with the notice provisions required by PACA, PACA trust protection can help you if the buyer files for bankruptcy. PACA trust protection means that certain of the buyer's assets should be protected and only used to pay for the produce that the buyer purchased.<sup>56</sup> If the buyer files bankruptcy, these assets are not considered to be part of the bankruptcy estate.<sup>57</sup> They are supposed to be held in trust for the farmer until the entire purchase price has been paid.<sup>58</sup>

In order for produce farmers to benefit from the PACA trust protection, they must have complied with the notice requirements as part of the produce sale transaction (prior to the buyer filing bankruptcy). The PACA notice requirement is a written notice to the buyer of a seller's intent to preserve PACA trust benefits.<sup>59</sup> The PACA notice is often routinely included in farmers' invoices to buyers (a recommended practice).

To be effective, the PACA notice must be received by the buyer within 30 days from the date payment was due on a delivery or the date you received notice that a check from the buyer has been dishonored.<sup>60</sup> The notice must also be received prior to the buyer filing bankruptcy. For more information, see the PACA website at <http://www.ams.usda.gov/AMSV1.0/PACA> and click on "How to Preserve Trust Rights" for more information.

If you raise and/or sell livestock, swine, or poultry, the PSA provides a trust mechanism for certain unpaid livestock and poultry producers that ensures trust assets sufficient to pay the unpaid sellers remain separate from the buyer's bankruptcy estate. Keeping the trust assets separate from the estate means the trust assets cannot be used to pay the buyer's other creditors, so the unpaid livestock and poultry producers do not have to compete with the buyer's other creditors for payment.

The PSA trust mechanism requires both written notice and a court filing—generally before the buyer files bankruptcy. To benefit from the PSA trust, you must provide written notice to the packer or processor and GIPSA within 30 days of the final date for making prompt payment, or within 15 business days of being notified that a buyer's payment check was dishonored.<sup>61</sup> If you file a timely notice and a complaint in court, the court can order a packer whose average annual purchases of livestock exceed \$500,000 and a poultry processor whose average annual sales, purchases, or value of poultry raised under a growing agreement exceeds \$100,000 to hold specified property in trust for your benefit as an unpaid producer. You would then be paid from this trust without competing with the buyer's other creditors.

- *Timing of buyer's debts in bankruptcy*

Under bankruptcy law, it makes a difference when you sold your goods to the buyer and when the buyer was supposed to pay you. If the buyer was supposed to pay you a long time before the buyer files for bankruptcy, you will have an unsecured claim against the buyer's bankruptcy estate (meaning you will be one of the last in line to get paid) unless: (1) you have preserved your PACA or PSA rights as discussed above; or (2) you have perfected a statutory lien against livestock delivered to the buyer (if applicable).

If you sold your goods shortly before the bankruptcy filing, your claim may be categorized as a priority claim under § 507 of the Bankruptcy Code. This section provides some priority to debts for sellers of products that were delivered in the ordinary course of business to the buyer within 20 days before the petition was filed.<sup>62</sup> This means that, if there is money available, you could be paid before the buyer's general unsecured creditors—but after the secured creditors.<sup>63</sup>

If you continue to sell your goods to the buyer after it has filed bankruptcy, you should be certain that the sale is authorized under the Bankruptcy Code. In some cases, it may have to be approved by the bankruptcy court, and the buyer will need to reaffirm your contract. In this case, however, payment to you should be treated as a priority expense, and you will be paid before almost all others.

Again, bankruptcy law is extremely complex. Be sure to consult a bankruptcy attorney if you are dealing with a buyer who has become insolvent or filed for bankruptcy.



## ORGANIC FARMER BREACHES

### Failure to Deliver

If you fail to deliver as promised in a contract, first look to see what the contract says about the situation. If it says nothing, or is unclear, the buyer may be able to:

- Recover any money already paid to you under the contract.<sup>64</sup>
- Deduct any costs the buyer incurs due to your lack of delivery from any other payments owed to you under the same contract.<sup>65</sup>
- Cancel the contract.<sup>66</sup>
- Buy similar goods from another farmer. The legal term for this is “cover.”<sup>67</sup>
- Sue you for damages. Damages could be measured in two ways, based on whether the buyer buys replacement products:
  - (1) If the buyer does cover, any amount the buyer had to pay for the replacement products above the contract price, plus incidental or consequential damages (defined below), minus any savings realized from your failure to deliver.<sup>68</sup>
  - (2) If the buyer does not cover, the difference between the contract price and the organic market price, plus incidental or consequential damages, minus any savings.<sup>69</sup>
- Take the contracted goods from you (assuming you have them), if they are unique or the buyer cannot cover.<sup>70</sup>

A buyer’s incidental damages include commercially reasonable expenses in connection with buying replacement products, and any other reasonable expenses resulting from your breach.<sup>71</sup>

A buyer’s consequential damages include any financial loss resulting from not receiving products that meet the buyer’s particular requirements, if the farmer knew about the requirements and there are no replacement products available that satisfy the requirements.<sup>72</sup>

You may have a defense to a failure-to-deliver breach if it is commercially impracticable for you to deliver. This could happen if the products are destroyed without the fault of either party before the risk of loss passes to the buyer, or if something happens that negates a basic assumption upon

which the contract was made.<sup>73</sup> Commercial impracticability generally means something that could not have been foreseen at the time the contract was signed, and generally does not include price fluctuations. Examples of commercial impracticability include war, embargo, crop failures, and failure of a major source of necessary supplies.

### **Failure to Meet Contract Quality Standards**

If you are unable to deliver products that meet the buyer's quality standards, first look to see what the contract says about this situation. If it says nothing, or is unclear, the buyer may be able to:

- Reject some or all of the products (within a reasonable time).<sup>74</sup>
- Recover any money already paid to you under the contract.<sup>75</sup>
- Deduct any damages incurred due to your failure to meet the quality standards from any payments owed to you under the same contract.<sup>76</sup>
- Cancel the contract.<sup>77</sup>
- Reject the products, buy similar products from another farmer (cover), and sue you for any extra amount the buyer had to pay above the contract price, plus incidental or consequential damages (defined on the previous page), minus any savings.<sup>78</sup>
- Accept the lower-quality goods, and dock or sue you for the difference between the value of the goods accepted and the value they would have had if they had met quality standards, plus any incidental or consequential damages.<sup>79</sup>
- Sell lower-quality goods in the buyer's possession, if at least partially paid for, to cover the buyer's costs. The buyer can do this without technically "accepting" the goods under the contract.<sup>80</sup>
- Take the contracted goods from you (assuming you have them), if they are unique or the buyer cannot cover, and pay you a reduced amount based on the lower quality.<sup>81</sup>

Your contract may set out alternative remedies to the options listed here. Also, whether or not it is set out in the contract, you may be able to provide the buyer with substitute products that do meet the quality standards (assuming you have them) if you notify the buyer of your intent to do so, and either: (1) the contract time has not yet expired; or (2) you had reasonable grounds to believe that the original products would be acceptable and you deliver substitute products meeting the quality standards within a reasonable time.<sup>82</sup> To substitute products, you would

likely have to either provide another portion of your crop that meets the contract quality standards (including proof of organic certification) or purchase suitable commodities on the spot market.

If the buyer rejects your products, it may have a duty to care for them long enough to permit you to remove them. If you have no agent or place of business at the rejection site, the buyer may be required to follow your reasonable instructions for transferring or disposing of the products. If you fail to give instructions, the buyer may be further required to make reasonable efforts to sell the goods for your account if they are perishable or threaten to quickly decline in value. You would likely be required to compensate the buyer for all of these efforts.<sup>83</sup>

### **Farmer's Repudiation**

If, for some reason, you need or want to repudiate the contract (that is, tell the buyer, before delivering products, that you will not be fulfilling your contract promises), be sure to check what the contract says about repudiation. You can repudiate with respect to all or a portion of the products under contract. If the contract says nothing about repudiation, or is unclear, the buyer may be able to:

- Recover any money already paid to you under the contract.<sup>84</sup>
- Deduct from any other payments owed to you under the same contract any damages the buyer incurs due to your failure to fulfill your promises.<sup>85</sup>
- Cancel the contract.<sup>86</sup>
- Buy similar goods from another farmer (cover).<sup>87</sup>
- Sue you for damages. Damages could be measured in two ways, based on whether the buyer buys replacement products:
  - (1) If the buyer does cover, any amount the buyer had to pay for the replacement products above the contract price, plus incidental or consequential damages (defined on page 12–25 of this chapter), minus any savings realized from your repudiation.<sup>88</sup>
  - (2) If the buyer does not cover, the difference between the contract price and the organic market price, plus incidental or consequential damages, minus any savings.<sup>89</sup>
- Take the contracted goods from you (assuming you have them), if they are unique or the buyer cannot cover, and pay you the

contract price less any consequential or incidental damages your repudiation caused the buyer.<sup>90</sup>

### **Farmer's Failure to Perform Other Contract Promises**

If you are unable to perform one or more of your contract duties other than delivery of acceptable products, look to see what the contract says about the situation. If it says nothing, or is unclear, the buyer may be able to:

- Recover in any manner that is reasonable.<sup>91</sup> This could include suing you for money damages or asking a court to either stop you from doing something or force you to do something (by getting an injunction against you).

You may have a defense to your failure to perform certain contract promises. For example, some state laws and the federal Packers and Stockyards Act nullify some types of contract provisions (for example, broad confidentiality provisions). If you breach an organic contract and it becomes clear the buyer plans to take action against you, consult an attorney licensed to practice in your state to see what defenses you might have under state law or otherwise.

### **Farmer Files For Bankruptcy**

If your farm is experiencing financial distress, it is important to consider whether or not there are bankruptcy options that may help to restructure or reduce farm debts. For example, Chapter 12 of the Bankruptcy Code provides special reorganization options for family farmers. Careful pre-bankruptcy planning may be critical to the success of any bankruptcy case and can help manage contract obligations.

As discussed above, bankruptcy rules are complex and can override contract language. Farmers should consult a bankruptcy attorney familiar with farm bankruptcy (commonly referred to as "Chapter 12" bankruptcy) before a debt situation becomes too severe.

**CHAPTER 12 — ENDNOTES**

- <sup>1</sup> Minn. Stat. § 17.710 (2012).
- <sup>2</sup> 7 U.S.C. §§ 499a-499s. See also U.S. Department of Agriculture PACA website at [www.ams.usda.gov/PACA](http://www.ams.usda.gov/PACA) and the National Agricultural Law Center PACA Reading Room at <http://www.nationalaglawcenter.org/assets/overviews/perishablecommodities.html>.
- <sup>3</sup> See generally 7 C.F.R. § 46.2(aa) (2012).
- <sup>4</sup> In re Craig-Ann Hunts Point Corporation, 50 Agric. Dec. 1850 (U.S.D.A. 1991); In re Baltimore Tomato Company, Inc., 39 Agric. Dec. 412 (U.S.D.A. 1980). Farmers should consult an attorney licensed to practice in their state about how partial payment might affect any related state law claims.
- <sup>5</sup> See 7 U.S.C. §§ 499e(a), 499f(a) (2012); 7 C.F.R. §§ 47.2, 47.3 (2012).
- <sup>6</sup> See 7 U.S.C. §§ 499c, 499d, 499f, 499h, 499i, 499m (2012); 7 C.F.R. § 46.45 (2012).
- <sup>7</sup> 7 U.S.C. §§ 181-231 (2012).
- <sup>8</sup> The Packers and Stockyards Act (PSA) includes specific regulations for livestock, poultry and swine producers.

For livestock and poultry producers who do business with packers and processors covered by the PSA, the PSA rules also include detailed provisions addressing such matters as: (1) setting a deadline for prompt payment for cash sales and under production contract growing arrangements, 9 C.F.R. § 201.43 (2012); (2) requiring the weighing of livestock and poultry delivered for slaughter and of any feed provided by a packer or processor, 9 C.F.R. §§ 201.55, 201.108-1, 201.82 (2012); and (3) requiring explicit contract language allowing producers to choose not to be covered by an arbitration provision in the contract and setting criteria that the U.S. Department of Agriculture (USDA) will consider when determining whether an arbitration provision in a contract violates the PSA, 9 C.F.R. § 201.218 (2012).

For growers raising swine or poultry under production contract growing arrangements, the PSA rules also establish criteria that USDA will use when determining whether a swine contractor or poultry processor has violated the PSA by: (1) requiring the producer to make additional capital investments in equipment or facilities during the life of the growing arrangement, 9 C.F.R. § 201.216 (2012); or (2) failing to give the producer a reasonable time to correct a breach of contract that might lead to termination of that contract, 9 C.F.R. § 201.217 (2012).

Poultry processing companies covered by the PSA must also: (1) give the producer the contract language at the same time specifications for the poultry houses are given; (2) allow the producer to discuss offered contract provisions with state or federal agency staff, family members, financial and legal advisors, lenders, and other producers raising birds for the same processor; (3) give the grower a written contract that clearly spells out specified provisions, including those related to the duration of the contract, all payment information, and performance or improvement plans; (4) include in the settlement sheet information that explains how the producer's pay on each

flock was calculated; and (5) provide written notice of contract termination, 9 C.F.R. § 201.100 (2012).

The PSA rules also establish criteria that USDA will use when determining whether a processor has given a poultry producer reasonable notice before suspending delivery of birds, 9 C.F.R. § 201.215 (2012).

- <sup>9</sup> The Packers and Stockyards Act uses the term “live poultry dealer” to refer to companies that either purchase poultry for slaughter or enter into production contracts with producers to raise birds that the company owns. This guide uses the term “poultry processor” instead of “live poultry dealer.”
- <sup>10</sup> 7 U.S.C. § 192 (2012).
- <sup>11</sup> See, for example, *Pickett v. Tyson Fresh Meats, Inc.*, 420 F.3d 1272 (11th Cir. 2005), cert. denied, 126 S.Ct. 1619 (2006) (holding that “unfair” practices proscribed by the Packers and Stockyards Act (PSA) are those that do or are likely to adversely affect competition); *Adkins v. Cagle Foods JV, LLC*, 411 F.3d 1320, 1326-27 (11th Cir. 2005) (affirming summary judgment for processor where producers did not produce sufficient evidence for the PSA claim to go to the jury); *Mims v. Cagle Foods, JV, LLC*, 148 Fed. Appx. 762, 767-69 (11th Cir. 2005) (same); *Wheeler v. Cagle Foods JV, LLC*, 148 Fed. Appx. 760, 762 (11th Cir. 2005) (same); *London v. Fieldale Farms Corp.*, 410 F.3d 1295, 1303 (11th Cir. 2005), cert. denied, 126 S.Ct. 752 (holding that to succeed on a claim under the PSA, a plaintiff must show that the defendant's unfair, discriminatory, or deceptive practice does or is likely to adversely affect competition).
- <sup>12</sup> In this discussion of the Packers and Stockyards Act, this guide uses the term “grower” to refer to those who raise poultry or swine owned by a poultry processor or swine contractor under what is referred to as a growing arrangement or production contract.
- <sup>13</sup> 9 C.F.R. §§ 201.27-201.42 (2012).
- <sup>14</sup> 7 U.S.C. §§ 2301-2306 (2012).
- <sup>15</sup> See, for example, Testimony of Steven Etko, Submitted to U.S. Senate Committee on Agriculture, Nutrition and Forestry, 2012 Farm Bill Field Hearing (May 31, 2011), available at [www.nationalorganiccoalition.org/policycomments/NOC%20Testimony%202012%20Farm%20Bill%20Field%20Hearing,%20Lansing,%20MI.pdf](http://www.nationalorganiccoalition.org/policycomments/NOC%20Testimony%202012%20Farm%20Bill%20Field%20Hearing,%20Lansing,%20MI.pdf).
- <sup>16</sup> See, for example, Rural Advancement Foundation International-USA, *Contract Agriculture Policy Recommendations* (December 2008), available at <http://www.rafiusa.org/programs/contractag/transition.html> and [http://www.rafiusa.org/docs/ag\\_fair\\_practices\\_act.pdf](http://www.rafiusa.org/docs/ag_fair_practices_act.pdf).
- <sup>17</sup> For a detailed overview of state laws related to agricultural production contracts, see Alison Peck, *State Regulation of Production Contracts* (The National Agricultural Law Center, May 2006), available at [http://www.nationalaglawcenter.org/assets/articles/peck\\_contractregulation.pdf](http://www.nationalaglawcenter.org/assets/articles/peck_contractregulation.pdf). Because the laws may have changed since the publication of this article, consult an attorney or check the individual state statutes and case law for the most up-to-date information.
- <sup>18</sup> See Arkansas Livestock and Poultry Contract Protection Act, Ark. Code Ann. § 2-32-201 (2012).

- <sup>19</sup> See Ga. Code Ann. §§ 2-22-1 to 2-22-5 (2012).
- <sup>20</sup> See Kan. Stat. Ann. §§ 16-1501 to 16-1506 (2012) (swine); Kan. Stat. Ann. § 16-1701 (2012) (poultry).
- <sup>21</sup> See Illinois Agricultural Production Contract Code, 505 Ill. Comp. Stat. §§ 17/1-17/99 (2012); see also Office of the Attorney General for the State of Illinois, *Agricultural Production Contract Code and Guidelines* (2005), available at <http://illinoisattorneygeneral.gov/environment/agprodguide.pdf>.
- <sup>22</sup> See Iowa Code Ann. §§ 202.1-202.5; 714.8; 714.11; 579B.1-579B.7; 654B.1-654B.11 (2012).
- <sup>23</sup> See Minn. Stat. §§ 17.90-17.98 (2012); see also Minnesota Wholesale Produce Dealers Act, Minn. Stat. §§ 27.001-27.20 (2012).
- <sup>24</sup> See Wis. Admin. Code (Agriculture, Trade, & Consumer Protection (ATCP)) §§ 101.01-101.07 (2012); Wis. Stat. § 100.04 (2012).
- <sup>25</sup> See Cal. Food & Agric. Code §§ 55631-55635 (2012) (upon delivery, producer lien attaches to all farm products in possession of processor, and has priority over most other liens).
- <sup>26</sup> Minnesota Wholesale Produce Dealers Act, Minn. Stat. §§ 27.001-27.20 (2012).
- <sup>27</sup> See, for example, U.C.C. § 2-719, comment 1 (1977) (“parties are left free to shape their [own] remedies”).
- <sup>28</sup> See U.C.C. §§ 2-703(a), (b), 2-705 (1977).
- <sup>29</sup> See U.C.C. § 2-703(f) (1977).
- <sup>30</sup> See U.C.C. §§ 2-703(d), 2-706 (1977).
- <sup>31</sup> See U.C.C. §§ 2-703(d), (e), 2-706 (1977).
- <sup>32</sup> See U.C.C. §§ 2-703(e), 2-708(1) (1977).
- <sup>33</sup> See U.C.C. §§ 2-703(e), 2-708(2) (1977).
- <sup>34</sup> See U.C.C. § 2-710 (1977).
- <sup>35</sup> See 7 U.S.C. §§ 209(a), 208(b) (2012).
- <sup>36</sup> See U.C.C. §§ 2-703(a), (b), 2-705 (1977).
- <sup>37</sup> See U.C.C. § 2-703(f) (1977).
- <sup>38</sup> See U.C.C. §§ 2-703(d), 2-706 (1977).
- <sup>39</sup> See U.C.C. §§ 2-703(d), 2-706 (1977).
- <sup>40</sup> See U.C.C. §§ 2-703 (e), 2-709 comment 2 (1977).
- <sup>41</sup> See, for example, Cal. Food & Agric. Code §§ 55631-55634 (2012); Iowa Code § 579B.1-579B.7 (2012).
- <sup>42</sup> See 7 U.S.C. §§ 196, 197 (2012).
- <sup>43</sup> See U.C.C. §§ 2-703(a), (b), 2-705 (1977).
- <sup>44</sup> See U.C.C. § 2-703(f) (1977).

- <sup>45</sup> See U.C.C. §§ 2-703(d), 2-706 (1977).
- <sup>46</sup> See U.C.C. §§ 2-703(d), 2-706 (1977).
- <sup>47</sup> See U.C.C. §§ 2-703(e), 2-708(1) (1977).
- <sup>48</sup> See U.C.C. §§ 2-703(e), 2-708(2) (1977).
- <sup>49</sup> See 7 U.S.C. §§ 499e(a), 499f(a) (2012); 7 C.F.R. §§ 47.2, 47.3 (2012).
- <sup>50</sup> See 7 U.S.C. § 192 (2012).
- <sup>51</sup> You would sue the buyer under common law contract principles, and could also have a remedy for incidental damages under U.C.C. § 2-715 (1977).
- <sup>52</sup> See 7 U.S.C. §§ 499c, 499d, 499f, 499h, 499i, 499m (2012); 7 C.F.R. § 46.45 (2012).
- <sup>53</sup> See 7 U.S.C. § 192 (2012).
- <sup>54</sup> See U.C.C. § 2-702(1) (1977).
- <sup>55</sup> See U.C.C. § 2-702(2), (3) (1977).
- <sup>56</sup> The PACA trust amount cannot be used by the buyer for any other expense or debt, and the farmer can be paid before any of the buyer's other creditors, even if there are not enough assets to cover all of the buyer's debt. See *Continental Fruit Co. v. Gatzliolis & Co.*, 774 F. Supp. 449, 453-54 (N.D. Ill. 1991) (holding that PACA seller's interest trumps nearly all others). See also *In re Kornblum & Co., Inc.*, 81 F. 3d 280, 286 (2nd Cir. 1996) (holding all assets of produce buyer which are derivatives or proceeds of produce form single PACA trust which exists for benefit of all produce sellers and which continues in existence until all of outstanding beneficiaries have been paid in full).
- <sup>57</sup> See *In re Al Nagelberg & Co.*, 84 B.R. 19, 21 (Bankr. S.D.N.Y. 1988) (holding that assets held in trust under PACA are not part of bankrupt debtor's estate).
- <sup>58</sup> If there has been wrongful diversion of trust assets, and if those assets can be traced into another asset held by debtor, the new asset may be impressed with a constructive trust under ordinary trust principles, even though it might be impossible to recover trust monies paid for such asset from bona fide purchaser for value. In *re Al Nagelberg & Co.*, 84 B.R. 19, 21-22 (Bankr. S.D.N.Y. 1988) (holding that where debtor, wholesale receiver, and seller of perishable foods utilized proceeds of fruits and vegetables subject to PACA trust to purchase three stores at time when it had unpaid vendors, U.S. Department of Agriculture may impose trust upon proceeds of sale of such stores).
- <sup>59</sup> See 7 U.S.C. § 499e(c); 7 C.F.R. § 46.46 (2012).
- <sup>60</sup> See 7 U.S.C. § 499e(c) (2012); 7 C.F.R. § 46.46 (2012).
- <sup>61</sup> See 7 U.S.C. §§ 196, 197 (2012).
- <sup>62</sup> See 11 U.S.C. § 503(b)(9) (2012).
- <sup>63</sup> See 11 U.S.C. § 507(a)(2) (2012).
- <sup>64</sup> See U.C.C. § 2-711(1) (1977).
- <sup>65</sup> See U.C.C. § 2-717 (1977).



- <sup>66</sup> See U.C.C. § 2-711(1) (1977).
- <sup>67</sup> See U.C.C. § 2-711(1)(a) (1977).
- <sup>68</sup> See U.C.C. §§ 2-711(1)(a), 2-712 (1977).
- <sup>69</sup> See U.C.C. §§ 2-711(1)(b), 2-713 and comment 5 (1977).
- <sup>70</sup> See U.C.C. §§ 2-711(2)(b), 2-716 (1977).
- <sup>71</sup> See U.C.C. § 2-715(1) (1977).
- <sup>72</sup> See U.C.C. § 2-715(2) (1977). The law does not currently recognize consequential damages for sellers. This is the case under the unamended version of Article 2 that has been adopted in every state but Louisiana. Under the revised Article 2 proposed in 2003, sellers would also be eligible for consequential damages. However, revised Article 2 has not been adopted in any state.
- <sup>73</sup> See U.C.C. §§ 2-613, 2-614, 2-615 (1977).
- <sup>74</sup> See U.C.C. §§ 2-601, 2-602 (1977).
- <sup>75</sup> See U.C.C. § 2-711(1) (1977).
- <sup>76</sup> See U.C.C. § 2-717 (1977).
- <sup>77</sup> See U.C.C. § 2-711(1) (1977).
- <sup>78</sup> See U.C.C. §§ 2-711(1)(a), 2-712 (1977).
- <sup>79</sup> See U.C.C. § 2-714 (1977).
- <sup>80</sup> See U.C.C. §§ 2-711(3) and comment 2, 2-706 (1977).
- <sup>81</sup> See U.C.C. §§ 2-711(2)(b), 2-716 (1977).
- <sup>82</sup> See U.C.C. § 2-508 (1977).
- <sup>83</sup> See U.C.C. §§ 2-602, 2-603 (1977).
- <sup>84</sup> See U.C.C. § 2-711(1) (1977).
- <sup>85</sup> See U.C.C. § 2-717 (1977).
- <sup>86</sup> See U.C.C. § 2-711(1) (1977).
- <sup>87</sup> See U.C.C. § 2-711(1)(a) (1977).
- <sup>88</sup> See U.C.C. §§ 2-711(1)(a), 2-712 (1977).
- <sup>89</sup> See U.C.C. §§ 2-711(1)(b), 2-713 and comment 5 (1977).
- <sup>90</sup> See U.C.C. §§ 2-711(2)(b), 2-716 (1977).
- <sup>91</sup> See U.C.C. § 2-714, comment 2 (1977).

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