

Twelve Basic Rules of Contracting

ach experience with an agricultural production contract will be unique, depending on the nature of the relationship between the parties, the terms of the contract and the bargaining position of the parties. However a number of common principles to keep in mind are listed below.

- 1. Whoever wrote the contract took care of himself/herself. There is no reason to assume the contract being offered is fair or that your interests are protected. Although you may trust the company you are dealing with, production contracts are arm's length business transactions and must be considered in this light. This rule is especially important because you will usually be offered written contracts on a take-it-or-leave-it basis and given no real opportunity to negotiate the terms.
- 2. Read and understand any contract before signing it. Contract terms play a fundamental role in determining the rights and duties of the parties. A good example is understanding the difference between a bushel contract, which commits you to delivering a fixed amount regardless of the crop actually raised, and an acreage contract, which promises delivery of whatever amount is raised on a designated number of acres. If the terms of a contract are unclear, you need to ask questions until you understand it. You should consider having your attorney review the contract, especially if it involves a sizable portion of your production or involves a long-term relationship or investment. Legal advice is an investment, not a cost, when it resolves confusion and helps you avoid unfavorable economic consequences.
- **3.** Compliance with contract terms is required before the contract is performed. The price premiums you are expecting won't be paid unless the terms of the contract are satisfied. Failure to

- comply with the contract may subject you not just to lower returns but also to claims for damages, penalties for breach and other legal remedies. Producers who are unable to satisfy a contract requiring delivery of a fixed number of bushels might be surprised to learn they have to enter the market and buy higher-priced commodities to satisfy the contract.
- 4. Never assume that your failure to perform the contract will be excused. Under certain circumstances, you might think it reasonable to assume the other party will not require you to perform the agreement. Never make this assumption, especially if your failure to perform can be expected to cause the other party damages. If you do not think you will be able to perform or if you would like to amend the terms of the agreement, communicate with the other party rather than surprising them.
- **5.** Know the other party's financial situation and performance history. This knowledge is essential to ensure that you will be paid for what you deliver. This is especially important when the contract calls for the passage of legal title upon delivery or when there is a delay in the payment. In these cases, you become the other party's creditor, and in most situations your claim is unsecured other than by the contractual promise to pay. Before signing a contract, ask yourself what will happen if the buyer goes out of business or doesn't pay.
- 6. Weigh the advantages of the contract in terms of higher prices against any increased costs or risks. While a proposed production incentive, such as a \$2 a bushel premium for growing a specialty crop may appear attractive, you must also calculate the real costs and risks of the contract. Remember that the premium is in exchange for something. Perhaps the variety of grain being raised has a significant yield penalty.

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- 7. Proposed contracts are always subject to negotiation. While most production contracts will be printed on typed forms offered on a take-it-or leave-it basis, you do have the freedom to negotiate. A term that is in writing can still be changed if both parties agree to do so. Of course, your ability to obtain more favorable terms will depend on your market power to negotiate with the company and whether other growers are willing to sign the contract.
- **8.** If there are any changes in the agreement, make sure they are in writing and separately signed by the company representative. The fact that you believe the contract was amended doesn't mean it was. Most contracts specifically provide that the only thing enforceable is what is in writing.
- **9. Do not rely on oral communications made by the company**, either before the contract is signed or during performance. If what is being said is important to the relationship, be sure it is put in writing, signed by both parties and incorporated as an amendment to the contract. If you cannot get it in writing, be sure to keep copies of any documents, such as letters, payment sheets and checks, that you can use to show what was agreed.
- 10. Keep good records of your performance. It is always a good idea to keep good records when legal issues are involved. This is especially true in the performance of production contracts. Keep a record of all communication and contact with the contractor, and keep a record of your actions in producing the commodity. If possible, you should keep samples of what was produced and the results of independent quality tests, such as on the germination of seeds or the quality of produce. These records may come in handy in a later dispute over your compliance with the contract terms.

- 11. Don't hesitate to ask questions when you don't understand what is happening. Remember, you are committing yourself to performing under the terms of the written agreement. If you do not fully understand what the language means or how the procedure will operate, ask questions. The questions should be directed to the company representative or to your own advisers.
- 12. Stay in touch with the other party to the contract. Communication is important in resolving uncertainty and in preventing misunderstandings. Communication with the other side about your performance, questions or concerns lets you help build a smooth, productive relationship. When long periods pass without communication, it is possible for circumstances to change and put performance of the agreement in a much different light.