USDA GIPSA Final Rule on 2008 Federal Farm Bill Contracting Requirements Goes Into Effect on February 7, 2012.
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In the Dec. 23 Communicator, we summarized the final rule on federal swine and poultry contracting requirements that was announced by the USDA Grain Inspection, Packers and Stockyards Administration (GIPSA) on Dec. 8 and published in the Federal Register on Dec. 9. The final rule goes into effect on February 7, 2012 and applies to contracts "entered into, amended, altered, modified, renewed or extended" after that date. (Click here for a copy of the final rule.)

The Dec. 23 article summarized the final rule, the primary differences between the final rule and proposed rule, and noted GIPSA's responses to some of the major comments received, including those made by IPPA. This article, as well as presentations at the Iowa Pork Congress, will cover the effect of the final rule on contracts signed, amended, renewed or extended after February 7, 2012 and the steps swine contractors and contract growers should consider before and after that date regarding their contracts.

As noted in the Dec. 23 article, the final rule does not change the current GIPSA legal actions penalizing packers and contractors for failing to have disclosures in contracts regarding arbitration and court venue clauses, as well as legal actions against contractors for failing to have disclosures regarding the three-day right to cancel contracts and additional large capital investment requirements. Contractors must continue to review their contracts entered into, amended, altered, modified, renewed or extended after June 18, 2008 for compliance with these requirements.

The final rule implements the following sections regulating contracting requirements of the 2008 Farm Bill for swine production and marketing contracts:

- Additional capital investments criteria.
- Reasonable period of time to remedy a breach of contract.
- Arbitration.

It is important to note that each section of the final rule sets out criteria that GIPSA *may* consider in determining if there is a violation and each section states that "these criteria include, but are not limited to" the specific criteria listed. In other words, the rule itself doesn't give a complete list of what a swine producer must do to comply with the regulations. The effect of GIPSA's broad discretionary language is that the rule allows GIPSA to use criteria in each of the three sections in addition to the listed criteria and producers and others subject to the rules cannot be certain what criteria they must follow to comply with the rules.

Additional Capital Investments Criteria. This section applies to swine and poultry production contracts. Other than including the disclosures as noted previously in this article, contractors do need to include any specific contract language to comply with this section of the rule. Producers should review the rule definition of additional capital investment (in essence, "a combined amount of $12,500 or more per structure") and the criteria GIPSA may consider to determine if there is a violation. If a contract requires additional capital investments, contract language must

conform to those criteria. More importantly, regardless of whether the contract requires additional capital investments, these criteria should be reviewed at the time of any additional capital investment and the contractor and contract grower should sign a contract addendum which lists each criteria in the rule, and any others that may be applicable, and which states that the criteria have been reviewed and complied with, including the criteria that the grower had discretion to decide against the investment.

Reasonable period of time to remedy a breach of contract. This section applies to swine and poultry production contracts. The criteria GIPSA may consider in determining whether a requirement that a swine production contract grower or poultry grower has been provided a "reasonable period of time to remedy a breach of contract that could lead to contract termination" include but are not limited to (these criteria do not apply where "food safety or animal welfare is concerned", but note that GIPSA did not exclude environmental emergencies):

1. Whether the grower was provided written notice of the breach upon initial discovery of the breach if the other party to the contract intends to take an adverse action, including termination, against the grower.
2. Whether the notice of breach includes:
    a. A description of the act or omission believed to be a breach, including the contract believed to have been breached.
    b. Date of the breach.
    c. Means by which the grower can satisfactorily remedy breach, if possible, based on the nature of the breach.
    d. A date that provides a reasonable period of time to remedy the breach, based on the nature of the breach.
3. Whether the contractor took into account the grower's ongoing responsibilities related to the raising and handling of the poultry or swine when setting the date to remedy the breach.
4. Whether the grower was given adequate time after the notice of breach to rebut the allegation of a breach.

Producers should review clauses in their contracts that govern default and the grower's right to remedy a breach based on these new rule requirements. This review should include:

- The amount of time provided to correct the breach/default after the grower receives written notice of the default, before the contract can be terminated. The primary question raised by the rule is whether that period of time is reasonable for the specific situation.
- Producers must be able to show that they "took into account" the grower's "ongoing responsibilities related to the raising and handling" of the hogs under contract when they established the time period for correcting the default. See section 3 above.
- As noted in section 4 above, one criteria is whether a grower was given adequate time to rebut the alleged breach after the notice was received. Very few contracts contain a clause giving a grower a specific period of time to rebut the alleged breach. As a practical matter, the opportunity to rebut the alleged breach is included in the time period to cure the default. However, as a result of this rule, producers may want to either establish a specific time period for rebutting the breach or specifically refer to the opportunity to rebut the breach when setting the time period to cure the breach.

- If a grower default occurs, the notice sent to the grower must contain all of the points set out in section 2 above. In addition, although not specifically required by the rule, contractors may want to include a deadline date for the grower to rebut the alleged breach and make sure this deadline is reasonable.
- As noted in section 1 above, if the contractor intends to take an adverse action against the grower (including termination) because of a breach, one criteria of reasonableness in the rule is whether the grower was provided written notice of the breach when the contractor initially discovered the breach. This criteria requires the contractor to balance maintaining a good working relationship with the grower by working to correct performance issues before sending written notice vs. complying with the rule. However, the rule is clear that waiting to send the written notice of breach may be used against the contractor by GIPSA in determining compliance with the rule.
- If the contract has a clause allowing the contractor to take action against the grower, such as termination, if there is an environmental problem, that clause must be carefully reviewed to make sure there is a reasonable period of time for remedy by the grower since the final rule does not exclude environmental events like it does food safety and animal welfare.

Arbitration. This section applies to all livestock or poultry marketing or production contracts. The Packers and Stockyards Act defines livestock as cattle, sheep, swine, horses, mules and goats.

Contractors using a contract that requires arbitration must first have the following clause on the signature page of the contract in "bold conspicuous print":

> *"Right to Decline Arbitration.* A poultry grower, livestock producer or swine production contract grower has the right to decline to be bound by the arbitration provisions set forth in this agreement. A poultry grower, livestock producer or swine production contract grower shall indicate whether or not it desires to be bound by the arbitration provisions by signing one of the following statements; failure to choose an option will be treated as if the poultry grower, livestock producer or swine production contract grower declined to be bound by the arbitration provisions set forth in this Agreement:
> I decline to be bound by the arbitration provisions set forth in this Agreement _____
> I accept the arbitration provisions as set forth in this Agreement_____"

The rule states that if neither option is signed, the grower or livestock producer will be deemed to have declined arbitration.

Second, contractors using a contract that requires arbitration must also have a clause that discloses sufficient information in bold conspicuous print describing:

1. All the costs of arbitration to be paid by the grower or producer.
2. The arbitration process.
3. Any limitations on legal rights and remedies.

This information must be described in such a manner as to allow the grower or producer to make "an informed decision on whether to elect arbitration for dispute resolution."

Finally, contractors and their attorneys should review the arbitration clause in the contract taking into account the criteria GIPSA may consider to determine if the clause violates the requirements set in the 2008 Farm Bill. Those criteria include but are not limited to:

1. Whether arbitration costs and time limits are reasonable.
2. Whether the grower or producer is "provided access to and opportunity to engage in reasonable discovery of information" held by the other party.
3. Whether arbitration is required only for disputes under the contract.
4. Whether a "reasoned, written opinion based on applicable law, legal principles and precedent for the award is required to be provided to the parties."

Under all three sections of the final rule, other than rule requirements that specifically require contract language, it is not clear when a violation of the rule would occur. Is a violation based on the contract language itself or is it when that contract language comes into play, such as when there is a breach of the contract. The safest course of action to comply with the rule is to try to make sure contract language is in compliance and then implement that contract language as required by the rule. However, it appears to be more critical to comply with the rule when a regulated event occurs, such as when an additional capital investment is required, when a breach of contract occurs, or when arbitration is required.

Again, this final rule goes into effect on February 7, 2012 and applies to contracts "entered into, amended, altered, modified, renewed or extended" after that date. Existing contracts that are not "amended, altered, modified, renewed or extended" after that date are not required to meet the requirements of the rule.

There are and will continue to be many questions about what the language of the criteria in the final rule actually means. We will provide additional information as these questions surface.

As with any legal issue, producers should consult an attorney for individual legal advice.