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# **Legal aspects of the life-cycle of agricultural production contracts. Critical issues for sustainable contract farming arrangements**

**Elissavet Tastsidou**

**SCHOOL OF ECONOMICS, BUSINESS ADMINISTRATION & LEGAL STUDIES**

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Student Name: Elissavet Tastsidou  
SID: 1104150052  
Supervisor: Prof. Anna Veneziano

I hereby declare that the work submitted is mine and that where I have made use of another's work, I have attributed the source(s) according to the Regulations set in the Student's Handbook.

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Thessaloniki - Greece

## **Abstract**

This dissertation was written as part of the LLM in Transnational and European Commercial Law, Mediation, Arbitration and Energy Law at the International Hellenic University.

Motivation for the present dissertation has been the recent publication of the Legal Guide on Contract Farming (July 2015) jointly drafted by UNIDROIT, FAO and IFAD. Contract farming is a new business model in the agricultural supply chain that meets great acceptance, notably because it entails important advantages for both participants: farmers' have improved access to markets, inputs and technical assistance, as regards their agricultural production, as well as a guaranteed income, whereas agribusinesses have a stable supply of agricultural products that meet their quality standards. This new business model is implemented through agricultural production contracts, which are agreements that generate certain legal issues and thus their approach is of great interest. The present dissertation analyzes four important issues: the role of third parties involvement in contract farming, the importance of quality standards for the implementation of agricultural production contracts, the legal effects of force majeure on contract farming and the enforcement mechanisms available in agricultural production contracts.

Furthermore, this dissertation attempts to highlight some critical issues that affect contract farming and can contribute to its success and further development. To this aim, deals with the role of public private partnerships, the contribution of agricultural insurance in contract farming arrangements and last but not least the financial mechanisms that can support this business model.

**Keywords:** agricultural production contracts, contract farming, sustainable growth, agricultural value chain, risk mitigation

Elissavet Tastsidou

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## **Preface**

I would like to express my gratitude to my supervisor Prof. Anna Veneziano for her support and feedback, as well as for her very helpful comments and recommendations.

I dedicate the present dissertation to my six-year old daughter, Iro

<b>ABSTRACT .....</b>	<b>3</b>
<b>PREFACE.....</b>	<b>4</b>
<b>CONTENTS.....</b>	<b>5</b>
<b>1. INTRODUCTION</b>	
<b>1.1 Basic elements of the concept of contract farming.....</b>	<b>6</b>
<b>1.2 A SWOT analysis of contract farming. Advantages and disadvantages.....</b>	<b>8</b>
<b>1.3 The legal regime of contract farming.....</b>	<b>11</b>
<b>CHAPTER 2 LEGAL ASPECTS OF THE LIFE CYCLE OF AGRICULTURAL PRODUCTION CONTRACTS</b>	
<b>2.1 PREFACE.....</b>	<b>13</b>
<b>2.2 The role of third parties involvement in contract farming.....</b>	<b>14</b>
<b>2.3 The importance of quality standards and specifications for the implementation of agricultural production contracts.....</b>	<b>17</b>
<b>2.4 The legal effects of force majeure on contract farming.....</b>	<b>21</b>
<b>2.5 Enforcement mechanisms in agricultural production contracts.....</b>	<b>25</b>
<b>CHAPTER 3 CRITICAL ISSUES FOR SUSTAINABLE CONTRACT FARMING ARRANGEMENTS</b>	
<b>3.1 PREFACE.....</b>	<b>27</b>
<b>3.2 Public private partnerships and contract farming.....</b>	<b>28</b>
<b>3.3 Agricultural insurance as a risk management tool in contract farming.....</b>	<b>32</b>
<b>3.4 Financing mechanisms of contract farming.....</b>	<b>36</b>
<b>CONCLUSIONS.....</b>	<b>40</b>
<b>BIBLIOGRAPHY</b>	

## INTRODUCTION

### 1.1 Basic elements of the concept of contract farming

The agricultural sector is the mainstay of many developed and developing countries as well, contributing decisively to their Gross Domestic Product (GDP), and therefore constitutes the driving force of many domestic economies<sup>1</sup>. This fact has given impetus to various countries worldwide to adopt modern agricultural policies, in an attempt to organize better their agricultural sector and promote agricultural economy. In this direction new methods and instruments have been developed which target to encourage the modernization of agriculture, increase productivity, enhance sustainable growth and ultimately transform agriculture into a competitive and profitable commercial activity.

Contract farming ranks among those methods that conduce to the evolution and modernization of agricultural production. Despite the fact that contracts between firms and farmers has been a well- known practice since the 19<sup>th</sup> century<sup>2</sup>, the phenomenon has been intensified during the recent decades. This is attributed to various reasons<sup>3</sup>: industrialization of agriculture, development of the supply chain management, world population growth, which in turn led to increased demand for food, trade and capital flows liberalization, improvement of transportation and logistics, progress in information technology. All these factors have amplified the implementation of contract farming, which is considered to be a successful tool for the promotion of the agricultural production and an effective method that succeeds to strike a balance between agricultural production capacity and increased market needs.

A plain definition would describe the concept of contract farming as agricultural production carried out by virtue of an agreement between a buyer and a farmer, which establishes conditions for the production and marketing of a farm product<sup>4</sup>. This succinct definition articulates the two basic elements of agricultural production

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<sup>1</sup> <http://data.worldbank.org/indicator/NV.AGR.TOTL.ZS?end=2014&start=1995&view=chart>

<sup>2</sup> Martin Prowse, Contract Farming in Developing countries, A. Savoir, Feb 2012, p 12

<sup>3</sup> Carlos A. da Silva, The Growing Role of Contract Farming in Agri- Food Systems Development: Drivers, Theory and Practice, FAO, AGSF, Agricultural Management, Marketing and Finance Service, [www.fao.org/fileadmin/user.../ags/.../AGSF\\_WD\\_9.pdf](http://www.fao.org/fileadmin/user.../ags/.../AGSF_WD_9.pdf)

<sup>4</sup> FAO 2012, Guiding principles for responsible contract farming operations, [www.fao.org/docrep/016/i2858e/i2858e.pdf](http://www.fao.org/docrep/016/i2858e/i2858e.pdf)

contracts: the agricultural production, namely farm products, and the binding agreement between at least two contracting parties (buyer and farmer)<sup>5</sup> having different but convergent interests in the object of the agreement, which is the agricultural production. One can easily understand that within the meaning of an agricultural production contract there are several other critical legal components such as volume, quality, price and timing of delivery of the agricultural products that supplement the notion of contract farming and render agricultural production contracts operational.

Taking into consideration the aforementioned elements, it could be submitted that agricultural production contracts are typical sales contracts. Nevertheless, the legal concept of contract farming encompasses some more crucial features that differentiate it from classical sales contracts<sup>6</sup>. Two further elements are most essential in agricultural production contracts: a) the contractual arrangement between the farmer and the buyer is for a fixed term and b) most of the times this arrangement takes place, before the production begins. The latter element is of high importance, as it enables the buyer to participate proactively to the production process by providing resources to the farmer, such as seeds, fertilizers, pesticides, young animals, veterinary products etc<sup>7</sup>, as well as by setting the conditions of the production and the specifications of the product<sup>8</sup>. Buyer's involvement in production can also take the form of financial support<sup>9</sup>. As agricultural production often requires large funds to be invested in tools, machinery, production equipment, irrigation systems etc small farmers can hardly meet the financial obligations that a large-scale agricultural production entails. Therefore, in many contract farming arrangements contractors provide financial support to the producer<sup>10</sup>

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<sup>5</sup> In literature the two basic contracting parties are also referred to as “contractor” and “producer”

<sup>6</sup> More analysis of how contract farming is different from direct sales contracts see UNIDROIT/FAO/IFAD, Legal Guide on Contract Farming, 2015, Introduction p. 2

<sup>7</sup> This type of agricultural production contracts is called resource – providing contracts where certain physical or technical inputs are provided by a firm, with the requirement that produce is marketed through the same firm, Martin Prowse, Contract Farming in Developing countries, A. Savoir, Feb, 2012, p 11

<sup>8</sup> This type of contract represents the production -management contract, where the firm stipulates and enforces conditions of production and farm-based processing, *ibid*, p. 11

<sup>9</sup> See more details in para 3.4

<sup>10</sup> UNIDROIT/FAO/IFAD, Legal Guide on Contract Farming, 2015, Introduction p. 4

safeguarding this way the financial viability of the agricultural production contract and achieving greater efficiency, as well as economies of scale.

Additional elements that frequently appear in agricultural production contracts constituting benchmarks, which distinguish contract farming from similar types of contracts, are related to the land property and the legal title on the production. More particularly, within the ambit of contract farming the farm products are produced on land owned or controlled by the farmer, whereas, generally, farmers have no legal title on the production, but the latter belongs exclusively to the contractor<sup>11</sup>.

The aforementioned analysis of the concept of contract farming highlights the basic elements that characterize contract farming arrangements and make them differ from similar forms of contracts. Obviously, an agricultural production contract can contain various other elements, depending on the will of the parties acting within the framework of the freedom of contracts. Hence, the scope of the contract can be broadened and more complex transactions can be established. This may be the case when third parties are getting involved in the agreement. The latter point is further discussed in para 2.2, as it is an issue that presents particular interest in contract farming constellations.

### **1.2 A SWOT analysis of contract farming. Advantages and disadvantages.**

In better understanding the philosophy as well as the implementation of contract farming, illustration of its stronger and weaker points would be most useful.

The concept of contract farming apart from its legal dimension<sup>12</sup>, simultaneously it represents a business model that demands careful planning and prudent decision - making. The following paragraphs attempt to outline the risks and benefits of contract farming, employing for this assessment process a method familiar to project management, namely the method of "SWOT analysis"<sup>13</sup>.

Contract farming entails numerous advantages for both farmers and buyers<sup>14</sup>. First of all, farmers, through contract farming arrangements, acquire guaranteed market

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<sup>11</sup> Martin Prowse, Contract Farming in Developing countries, A. Savoir, Feb 2012, p 12

<sup>12</sup> The legal vehicle of contract farming is considered to be the agricultural production contract

<sup>13</sup> SWOT stands for Strengths, Weaknesses, Opportunities and Threats. More information on the issue: <https://www.projectsmart.co.uk/swot-analysis.php>

<sup>14</sup> Neil Hamilton, Farmer's Legal Guide to Production Contracts, 1995, The National Agricultural Law Center, University of Arkansas, p.14

access, improved access to inputs<sup>15</sup>, as well as technological assistance and know-how, factors that promote their inclusion to agricultural value chains. Furthermore, they are offered specialized services, such as standardization of products, transportation, logistics etc. As a chain-effect farmers' uncertainty regarding prices is reduced, their income is stabilized and their access to credits is enhanced. As far as the benefits for buyers are concerned, purchasing firms have a guaranteed supply of agricultural products that meet their specifications regarding quality, quantity and timing of delivery<sup>16</sup>. Contract farming can reduce input and labour costs, can facilitate access to land, enables the contraction or expansion of production according to the circumstances and also guarantees greater conformity to product quality attributes and to safety standards<sup>17</sup>. These entire benefits end up to a common denominator, which is probably the most significant advantage for both participants in contract farming arrangements, that is to say risk mitigation. Indeed, through contract farming, parties can avoid excessive risks by organising the production according to their true potential,<sup>18</sup> thus securing their interests and enhancing the viability of their businesses.

Despite these acknowledged benefits there are several weaknesses attributed to contract farming. Improper use of credit might lead to unsustainable levels of indebtedness for farmers<sup>19</sup>, especially in cases where they face production problems, or significant changes in market conditions occur, or simply the contractor does not honour its economic obligations of the contract<sup>20</sup>. Moreover, opportunistic behaviour on the part of purchasing firms can urge farmers in the long run to reduce their prices. The latter, combined with the fact that producers engaged in contract farming lose gradually their connection with market, puts farmers in disadvantageous position. The same risk applies also for purchasers, who, contracting with farmers through long-term contracts,

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<sup>15</sup> Martin Prowse, Contract Farming in Developing countries, A. Savoir, Feb 2012, p 24

<sup>16</sup> FAO <http://www.fao.org/ag/ags/contract-farming/faq/en/#c100445>.

<sup>17</sup> Carlos A. da Silva, The Growing Role of Contract Farming in Agri- Food Systems Development: Drivers, Theory and Practice, FAO, AGSF, Agricultural Management, Marketing and Finance Service, [www.fao.org/fileadmin/user.../ags/.../AGSF\\_WD\\_9.pdf](http://www.fao.org/fileadmin/user.../ags/.../AGSF_WD_9.pdf)

<sup>18</sup> UNIDROIT/FAO/IFAD, Legal Guide on Contract Farming, 2015, Introduction p.7

<sup>19</sup> Ibid, Legal Guide on Contract Farming, 2015, Introduction p.6

<sup>20</sup> Advantages and problems of contract farming :  
<http://www.fao.org/docrep/004/y0937e/y0937e03.htm>

lose their flexibility to seek alternative supply sources<sup>21</sup>. Another weak point that might derive from contract farming arrangements and raises concern for contractors is linked to land availability constraints. In cases, where producers' tenure rights are not secured, contractors might get entrapped, due to farmer- landlord disputes, endangering their interests<sup>22</sup>.

Alongside the aforementioned strong points of contract farming and despite its weaknesses the modern socio-economic environment creates new opportunities that can boost this business model of supply chain. Growth of population and urbanization combined with higher incomes and better live standards lead to increased demand for food and particularly for agricultural products<sup>23</sup>. Consumers' preference for agri-food is further corroborated by the growing public awareness, as well as by coordinated policies adopted by many governments that promote the concept of healthy living, wholesome diet and food safety. These conditions set the ground for large-scale agricultural production and to this direction contract farming arrangements are considered effective mechanisms to manage large transactions in the supply chain, so as markets can meet consumers' expectations as far as quantities and specifications of agricultural products are concerned. Moreover, the expansion of international trade coupled with progress in technology and information management, as well as development of transportation and logistics are enabling factors that conduce to the establishment of contract farming as a prevalent method of marketing agricultural production creating a favorable environment for its development.

Concluding the SWOT analysis of contract farming particular reference should be made to possible threats that might undermine this business method. Weak rule of law or lack of regulatory initiatives, unfavorable macro-economic framework conditions - as for example inflation, trading terms and fiscal policies<sup>24</sup> -, limited availability of funds and other financing tools are the major threats that might affect contract farming and inhibit its potential. Apart from these, the loss of biodiversity due to monoculture

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<sup>21</sup> UNIDROIT/FAO/IFAD, The Legal Dimension of Contract Farming, Bangkok, September 2014

<sup>22</sup> Advantages and problems of contract farming :  
<http://www.fao.org/docrep/004/y0937e/y0937e03.htm>

<sup>23</sup> Andrew Shepherd, An Introduction to Contract Farming, CTA, Technical Centre for Agricultural and Rural Cooperation, 2013, p.6

<sup>24</sup> Margrett Will, Contract Farming Handbook, GIZ 2013, p.26

production and the loss of local employment resulting from the introduction of sophisticated machines are reported as adverse factors for contract farming<sup>25</sup>.

### **1.3 The legal regime of contract farming**

Agricultural production contracts, from a legal point of view, are not a novel legal concept. As explained earlier, contract farming is an agreement based on the coincidence of the wills of at least two parties that have convergent interest in the production and marketing of a farm product. From this remark it can be deduced that for the determination of the legal framework of contract farming the existence of rules that govern contracts in general can suffice<sup>26</sup>. As contracts constitute core expression of the free will of the parties, in most legal systems there is an adequate legal framework that regulates contracts throughout their life-cycle. This legal framework normally consists of general provisions that delineate basic principles of contracts, as well as of more specific provisions that regulate more particular legal issues. It follows from the foregoing that in cases where a legal system has no special provisions for contract farming, contract law or law of obligations applies<sup>27</sup> guaranteeing adequate protection of the contractual relations between producers and buyers of agricultural products. Domestic agrarian codes might also have supplementary application for issues not covered by civil or contract law<sup>28</sup>. It goes without saying that when specific rules provide for mandatory contract requirements parties should respect these provisions from which they cannot deviate.

However, there are countries that have enacted a special legal regime for agricultural production contracts, in an effort to promote this new business method and in parallel to stimulate their agricultural sector. Morocco, Spain, India and the U.S.A are

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<sup>25</sup> Charles Eaton and Andrew Shepherd, *Contract Farming Partnerships for Growth*, FAO, 2001, p. 16

<sup>26</sup> Caterina Pultrone, *An Overview of Contract Farming: Legal Issues and Challenges*, [http://www.fao.org/fileadmin/user\\_upload/contract\\_farming/Uniform%20Law%20review\\_Pultrone.pdf](http://www.fao.org/fileadmin/user_upload/contract_farming/Uniform%20Law%20review_Pultrone.pdf)

<sup>27</sup> Marta Doria with contribution of Carlos da Silva, *Contract Farming: Legal Considerations on contractual design and enforcement*, FAO, [http://www.fao.org/fileadmin/user\\_upload/contract\\_farming/Brief%201%20legal%20aspects%20of%20contract%20farming.pdf](http://www.fao.org/fileadmin/user_upload/contract_farming/Brief%201%20legal%20aspects%20of%20contract%20farming.pdf)

<sup>28</sup> Henry Deeb Gabriel, *Contract Farming: A legal approach*, in *The Legal Dimension of Contract Farming*, IFAD, FAO, UNIDROIT, Bangkok, September 2014

among those legal systems that have ad hoc legislation on contract farming<sup>29</sup>. In such cases, the special legal regime prevails and contract law or law of obligations can be invoked, if unregulated issues arise.

Similar is the approach as regards agricultural production contracts that present international interest, namely when producer and contractor have places of business in different States. Despite the fact that parties may agree on the application of a specific national legal framework, critical factor for the determination of the applicable law is the existence of mandatory rules that indicate the application of the laws of a specific forum and which the parties cannot defy. In general, it can be submitted<sup>30</sup> that in international agricultural contracts, where parties have not expressed their preference as regards the applicable law, the law of the state where the farm products are produced applies, as this is deemed the characteristic performance of the contract.

Yet another issue that is very interesting, though contested, is whether in international agricultural production contracts the CISG<sup>31</sup> applies. Although contracts for farm products are not pure sale contracts, but, as explained earlier, encompass some essential elements that differentiate them, the fact that the CISG establishes uniform rules acknowledged by a notable number of contracting States, makes its influence significant even in contract farming arrangements<sup>32</sup>. Nevertheless, in each case the requirements of the CISG must be carefully examined and particular attention deserves Art. 3 of the CISG<sup>33</sup>, on the basis of which it is doubtful whether this international legal text applies in all types of agricultural production contracts<sup>34</sup>.

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<sup>29</sup><http://eba.worldbank.org/reports/~media/WBG/AgriBusiness/Documents/Reports/2015/EBA-2015-Contracting-agriculture-production.pdf>

<sup>30</sup> UNIDROIT/FAO/IFAD, Legal Guide on Contract Farming, 2015, Introduction p. 29

<sup>31</sup> CISG is the abbreviation of "United Nations Convention on Contracts for the International Sale of Goods". CISG Convention was adopted in Vienna in 1980 and as of May 2016, it has been ratified by 85 States.

<sup>32</sup> Caterina Pultrone, An Overview of Contract Farming: Legal Issues and Challenges, [http://www.fao.org/fileadmin/user\\_upload/contract\\_farming/Uniform%20Law%20review\\_Pultrone.pdf](http://www.fao.org/fileadmin/user_upload/contract_farming/Uniform%20Law%20review_Pultrone.pdf), p. 264, Uniform Law Review 2012 Vol XVII

<sup>33</sup> CISG Article 3: "(1) Contracts for the supply of goods to be manufactured or produced are to be considered sales unless the party who orders the goods undertakes to supply a substantial part of the materials necessary for such manufacture or production. (2) This Convention does not apply to contracts in which the preponderant part of the obligations of the party who furnishes the goods consists in the supply of labour or other services"

<sup>34</sup> Relevant the footnote 7

At any rate the issue of the applicable law in contract farming is a complex topic and the present dissertation only briefly touches upon some elements focusing on the typical two-partite relationship between the producer and the contractor. The situation over the applicable legal regime can be even more complicated, in cases where third parties participate in the contract having different interests, different obligations to perform and perhaps different nationalities<sup>35</sup>. Further analysis of these subjects escapes the scope of the thesis; suffices only to say that ultimately the judge assessing the circumstances, the preponderant obligation, as well as the mandatory or default provisions can determine the applicable legal regime that applies in a dispute arising from a particular agricultural production contract.

This introduction was indispensable for a better understanding of some basics on the concept of contract farming. The following chapters are dedicated to more specific issues, as the purpose of this dissertation is to highlight certain aspects of the life cycle of agricultural production contracts that present increased legal interest in the implementation of contract farming. Chapter 3 focuses on critical issues that can contribute to the dissemination of contract farming and may play a determinant role for its further success and effectiveness.

## **CHAPTER 2**

### **LEGAL ASPECTS OF THE LIFE CYCLE OF AGRICULTURAL PRODUCTION CONTRACTS**

#### **2.1 PREFACE**

Normally, all contracts follow a course of phases that usually comprises the stages of negotiation/exchange of information, formation, drafting/ signing, implementation/ performance and enforcement of the contract. This course illustrates a typical contract life-cycle. Within this life-cycle there is a plethora of factors, incidents and circumstances that may affect positively or negatively the contractual relations disturbing the balance of the contract or maximizing its efficiency and overall can have major impact on the contract.

The next paragraphs are dealing with specific legal issues that emerge during the stages of contract farming projects and merit attention, in the sense that their

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<sup>35</sup> More information on the legal treatment of agricultural production contracts is available in UNIDROIT/FAO/IFAD, Legal Guide on Contract Farming, 2015, Introduction p. 17-30

consideration can assist in designing and implementing sound and viable agricultural production contracts.

## **2.2 The role of third parties involvement in contract farming**

As has already been mentioned, apart from the traditional contracting parties, namely the producer and the contractor, third parties<sup>36</sup> can also participate in an agricultural production contract playing a major role in supporting the contract throughout its life-cycle.

The participation of farmers' organizations in agricultural production contracts is an important parameter that impacts primarily on the negotiation and formation phase of the contract.

It is well-known that in the domain of supply chain increased concentration and vertical integration of international retailers and food industries have led to structural changes that urged these economic actors to search for alliances and to seek economies of scale, in order to gain greater buying power and consequently considerable negotiating capacity<sup>37</sup>. In the context of contract farming individual farmers appear to be in a disadvantageous position, incapable to deal with this new development and counterbalance the enhanced bargaining power of their counter parties. Besides, contract farming requires relatively high levels of farm managerial skills, which farmers often lack<sup>38</sup>.

Best practices on contract farming have shown that producers associations or unions may contribute a lot to the efficiency of agricultural production contracts by exercising advocacy role, as well as by negotiating or signing contractual terms with buyers in the best interest of their members<sup>39</sup>. That practically means that producers associations possessing knowledge and relevant expertise have stronger negotiation and bargaining

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<sup>36</sup> According to Prof. Lawan Thanadsillapakul, third parties can be government agencies, private organizations, bank institutions, farmers associations etc, UNIDROIT/FAO/IFAD, *The Legal Dimension of Contract Farming*, Bangkok, September 2014

<sup>37</sup> Green Paper on unfair trading practices in the business to business food and non food supply chain in Europe, COM (2013), 37 (final)  
[eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=COM:2013:0037:FIN:EN:PDF](http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=COM:2013:0037:FIN:EN:PDF)

<sup>38</sup> Kanokwan Manorum, David Hall, Xing Lu, Suchat Katima, Maria Theresa Medialdia, Singkhon Siharath, and Pinwadee Srisuphan, *Cross-Border Contract Farming Arrangement: Variations and Implications in the Lao People's Democratic Republic*, 2011 Asian Development Bank, <https://www.adb.org/sites/default/files/publication/29172/cross-border-contract-farming.pdf>

<sup>39</sup> UNIDROIT/FAO/IFAD, *Legal Guide on Contract Farming*, 2015, p.65

power that enables them to take advantage of economies of scale, to reduce operational costs and succeed better prices, to have access to funds, capitals and technology, to better assess the risks and ultimately to improve the quality of production and the market access in favor of farmers<sup>40</sup>.

The above mentioned clearly illustrate that this parameter is of huge importance for agricultural production contracts, first and foremost because it conduces to the broadening of the scope of contract farming arrangements, in terms of contracting parties, as well as in terms of content, and moreover because it allows third parties to take active part in the contract negotiation and finally to conclude large scale agricultural production agreements to the benefit of their members, which otherwise might be involved in unfavorable situations to the detriment of their business activities.

Apart from the participation of producers associations in an agricultural production contract, insurers and certification agents may also contribute to the effectiveness of contract farming projects and their involvement in the contract can substantially facilitate the main actors, namely producers and contractors, to perform their obligations, while at the same time can add value to the content of the contract and its particular objectives.

The key concept of insurance is that of spreading risks. In other words, insurance is a form of risk management, primarily used to hedge against the risk of contingent loss (a potential loss dependent upon some future event occurring or not occurring). In essence, insurance is simply the equitable transfer of a risk of a loss from one entity, namely the insured person, to another (insurance company) in exchange for a premium, that is to say money paid to an insurance company for such protection<sup>41</sup>.

Within the ambit of agricultural production contracts, usual hazards that insurers are called upon to cover are fire, theft, disease, natural calamities, damage to property or injury of third parties on the facilities<sup>42</sup>. Insurers' involvement in the contract can be

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<sup>40</sup> Pari Baumann, Equity and Efficiency in Contract Farming Schemes: the experience of agricultural tree crops, 2000, Overseas Development Institute, p. 30-31

<sup>41</sup> Geoffrey Ombachi, Understanding the Role of Insurance in an economy, published on LinkedIn on June 3, 2015, <https://www.linkedin.com/pulse/understanding-role-insurance-economy-geoffrey-ombachi>

<sup>42</sup> UNIDROIT/FAO/IFAD, Legal Guide on Contract Farming, 2015, p.55

direct, when they participate actively therein, as contracting party, or indirect, when the insurance contract with one of the core contracting parties is separate, but interdependent with the requirements and obligations established by the agricultural production contract. As can be understood, in both situations the existence of an insurance scheme in a contract farming arrangement is of high importance, as practically serves as a safety belt towards inherent risks that contract farming entails and offers the financial protection needed, in order for the contract to be reliable and viable<sup>43</sup>.

In the same wavelength, parties' interests can best served by the participation of certification agents in the agricultural production contract. As it is outlined in the next paragraph, quality requirements of the agricultural production are essential component of contract farming arrangements, given that compliance with quality standards is a key-obligation and may affect parties' performance. In this regard, certification agents offer valuable services, such as on-site inspections of the production, sample –taking for quality tests, auditing and reviewing of relevant documents<sup>44</sup>. The involvement of quality professionals and experts in agricultural production contracts guarantees compliance with the standards stipulated in the contract and protects parties from irregularities and possible defects of the products, hence giving perspective to contract farming and a positive impact on this specific supply chain business model.

Other parties that may participate in the contract might be landlords, financial institutions, governments etc. By and large, any person or entity that might establish an interest in an agricultural production contract could contract. What it is worth stressing is that in all cases of third parties participation the contract is transformed into a multipartite agreement which, despite the fact that it creates more complex legal situations, facilitates the core parties, as ultimately the role of the additional actors is to ease the individual contracting parties of their burden of obligations<sup>45</sup>.

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<sup>43</sup> Further analysis of the importance of insurance in contract farming is provided in para 3.3

<sup>44</sup> UNIDROIT/FAO/IFAD, Legal Guide on Contract Farming, 2015, p.56

<sup>45</sup> Ayelech Tiruwha Melese, Contract Farming: Business Models that Maximise the Inclusion of and Benefits for Smallholder Farmers in the Value Chain, Rev. dr. unif. 2012, p. 293-294

### **2.3 The importance of quality standards and specifications for the implementation of agricultural production contracts**

An interesting legal issue that is linked primarily to the implementation and performance of agricultural production contracts and consequently determines the range of parties' obligations relates to quality specifications of the products.

The term standards and specifications of products can be understood as agreed criteria by which a product, its technical and physical characteristics, and/or the process and conditions under which it has been produced or delivered can be assessed<sup>46</sup>. Further analysis of this notion indicates that there are standards that relate to the physical characteristics of products and also those relating to production, handling and processing designed to ensure that products meet certain desired characteristics<sup>47</sup>.

Within the context of contract farming contracts often provide that producers are obliged to meet certain quality criteria, so that the final product will have the agreed specifications and attributes. These quality criteria most often are determined by express terms within the agricultural production contract or can be contained in a special appendix to the contract, which is considered to be a practical and convenient method for determining quality requirements<sup>48</sup>. Whatever the method of stipulating quality specifications of the product, particular emphasis should be placed on the common understanding of these technical terms by both parties and to this direction the use of sufficiently precise terms or explanatory remarks may play important role for the avoidance of possible subsequent disputes.

From a legal standpoint the issue of quality criteria is much more complex when no specific contractual terms regarding quality specifications exist. There are certain jurisdictions where, in the absence of express provisions determining quality standards, default rules apply to define performance specifications<sup>49</sup>. By way of example there are

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<sup>46</sup> Nadvi, Khalid, and Frank Wältring( 2004), Making Sense of Global Standards, in Hubert Schmitz (ed.), Local Enterprises in the Global Economy, (Cheltenham: Edward Elgar), p. 56.

<sup>47</sup> John Humphrey, Olga Memedovic, Global Value Chains in the Agrifood Sector, Unido 2006, [www.unido.org/fileadmin/user\\_media/Publications/Pub\\_free/Global\\_value\\_chains\\_in\\_the\\_agri\\_food\\_sector.pdf](http://www.unido.org/fileadmin/user_media/Publications/Pub_free/Global_value_chains_in_the_agri_food_sector.pdf)

<sup>48</sup> UNIDROIT/FAO/IFAD, Legal Guide on Contract Farming, 2015, p. 88

<sup>49</sup> <http://eba.worldbank.org/reports/~media/WBG/AgriBusiness/Documents/Reports/2015/>

various legal systems which, absent parties' agreement on the quality specifications of the product, require that the products should meet "contractor's reasonable expectations" or "current standards" or should conform to the "intended use". Furthermore, the widely acknowledged text of the Convention on Contracts for the International Sales of Goods (CISG) provides that, except if the parties have agreed otherwise, the seller must deliver goods that "are fit for the purposes for which goods of the same description would ordinarily be used or are fit for any particular purpose expressly or impliedly made known to the seller at the time of the conclusion of the contract, except where the circumstances show that the buyer did not or could not rely on the seller's skills and judgement to pursue this purpose by using the goods"<sup>50</sup>.

Notwithstanding that possible gaps in the contract may be filled by default rules, such those mentioned above, it cannot be overlooked that default rules are mostly vague notions that are susceptible to various legal interpretations and this fact, in turn, may lead to uncertainty, malfunctions in contract performance and ultimately to disputes. Thus, best practice in contract farming constellations, as regards quality specifications of the products, would be the drafting of precise terms and clauses, stipulating quality standards for the produced farm products in a clear-cut manner and leaving as less ground for recourse to default rules as possible<sup>51</sup>.

Two more elements deserve discussion as far as quality standards are concerned. The first is related to the increasing importance of private standards. Private quality standards can be set by private sector or civil society organizations in an effort to differentiate the products and to attach superior quality features thereto, guaranteeing conformity with safety, quality and environmental values<sup>52</sup>. Private standards have been important drivers for contract farming arrangements, in so far as producers are subject to constant monitoring and certification of their production until the final products meet

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EBA2015-Contracting-agriculture-production.pdf

<sup>50</sup> Art. 35 par.2 of the CISG

<sup>51</sup> UNIDROIT/FAO/IFAD, Legal Guide on Contract Farming, 2015, p. 89

<sup>52</sup> UNIDO (United Nations Industrial Development Organisation)

<https://www.unido.org/what-we-do/advancing-economic-competitiveness/o72296/private-standards.html?L=2%27A%3D0%3Ftx..>

the required quality<sup>53</sup> and that is essential for both parties. The certification and quality assurance schemes enable producers to use a specific logo or label on the product and this fact witnesses that products conform to the quality requirements of the contract. On the other side contractors are rest assured that the delivered products have been subjected to strict controls by expert certifying bodies and there is little risk of marketing unsuitable goods. Furthermore, in cases of non-conformity, certification agents may impose certain measures or sanctions<sup>54</sup> that have far-reaching implications for the performance of the contract, as contractual obligations and quality certification obligations are closely interdependent. Overall, private standards contribute a lot to rationalisation of agri-food supply chain; provide legal certainty for contract performance and thus add value to contract farming arrangements.

The second element is linked to food-safety standards and is high relevant to product quality. The increased demand of agricultural products globally has triggered wide concerns as regards the quality standards and the safety requirements of agri-food products. At the same time the fact that mandatory standards, as well as the stringency of those standards, increase renders the compliance with food safety requirements a complex issue. This complexity is further enhanced because of a shift from product standards towards controls over the way that products are grown, harvested, processed and transported<sup>55</sup>, hence safety standards have to be monitored at all these stages. On the other hand food safety is of utmost importance as far as consumers' health protection is concerned and requires that "food will not cause harm to the consumer when it is prepared and/or eaten according to its intended use"<sup>56</sup>. All these are real challenges that agri-food supply chain is required to deal with, so as to meet markets expectations and to establish reliable and trustworthy relations among the participants.

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<sup>53</sup>Private standards may also benefit producers through more efficient management, cost reduction, improved market access and enhanced product quality and corporate image, Pascal Liu, Trade and Markets Division, FAO, [http://www.fao.org/fileadmin/templates/est/AG\\_MARKET\\_ANALYSIS/Standards/Private\\_standards\\_\\_Trade\\_Liu\\_WTO\\_wkshp.pdf](http://www.fao.org/fileadmin/templates/est/AG_MARKET_ANALYSIS/Standards/Private_standards__Trade_Liu_WTO_wkshp.pdf)

<sup>54</sup> UNIDROIT/FAO/IFAD, Legal Guide on Contract Farming, 2015, p. 105

<sup>55</sup> John Humphrey, Global Value Chains in the Agrifood Sector, UNIDO, 2006 [https://www.unido.org/fileadmin/user\\_media/Publications/Pub\\_free/Global\\_value\\_chains\\_in\\_the\\_agrifood\\_sector.pdf](https://www.unido.org/fileadmin/user_media/Publications/Pub_free/Global_value_chains_in_the_agrifood_sector.pdf)

<sup>56</sup> Food Hygiene, Basic Texts, Fourth Edition, WHO/FAO, 2009, <http://www.fao.org/docrep/012/a1552e/a1552e00.pdf>

It is natural that an agricultural production contract, which is a mechanism that governs transactions within the supply chain, must also follow this demand and comply with food safety legislation.

In contract farming projects food safety issues present some interesting aspects, whose legal treatment is worth mentioning. As noted, food safety is strongly related to quality standards of the products and in this sense establishes contractual obligations, the breach of which may disturb the balance of the contract. Indeed, when the agricultural production contract contains provisions that specify safety standards for the final product, parties are obliged to uphold these specifications pursuant to the agreed stipulations, whereas the applicable law may fill gaps in case of default provisions. It should be stressed that food safety is a matter of public interest that raises the awareness of the State and thus food safety legislation in many legal systems is considered mandatory<sup>57</sup>. This means that parties in an agricultural production contract cannot derogate from this piece of legislation even though they may have agreed otherwise.

Special interest presents the legal approach of non contractual obligations that flow from an agricultural production contract and relate to food safety. When the produced agri-foods are considered unsuitable or unfit for human consumption the end consumer might sustain personal damage, which in turn has legal consequences, such as obligation for the restitution of the damage. One of the basic legal problems that might arise is who, of all operators within the supply chain, is deemed liable for compensation. General rules of tort law of the forum where the damage occurred might give the solution. Nevertheless, one should always be mindful that special provisions of food safety legislation might apply indicating the liable persons, which, depending on the ethic-sociological perceptions of the legislator and the grade of the intended protection, may extent from the farmer and other secondary operators until contractors and other facilitators. Similarly, when the agricultural production contract has an international dimension, in situations where the final consumer afflicted by an unsafe product is

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<sup>57</sup> <http://www.fao.org/food/food-safety-quality/capacity-development/food-regulations/en/>

located in a foreign country, consumers' domestic law should be examined, as issues related to consumers' health protection are enforced under domestic legislation<sup>58</sup>.

In general, food safety issues need careful consideration and legal treatment, because they entail serious risks that parties in an agricultural production contract, as well as other stakeholders within the supply chain, should assess, in order to be protected and mitigate or allocate the hazards in equitable and overall reasonable manner, without undermining the contract in total.

#### **2.4 The legal effects of force majeure on contract farming**

Contract performance is a key stage in the life-cycle of contracts, as, in essence, signifies the success or failure of the contract and respectively the parties, either discharge their obligations or pave the way for remedies due to breach of contract. Various events, causes and impediments may disturb the balance of the contract rendering its performance onerous, difficult or impossible. Changes in weather conditions, fluctuations in prices, political changes, a sudden disease or death or a simple breach of contract due to a specific behavior of one of the contracting parties are only some of the occasions that might affect the performance of the contract.

Force majeure is a legal notion encountered in many jurisdictions – notably civil law jurisdictions<sup>59</sup> - and constitutes a cause that often gives rise to transgression of obligations, hence leading many times to contract frustration<sup>60</sup>. It is widely acknowledged in international contractual relationships and thus the inclusion of “force majeure provisions” in international legal texts becomes all the more frequent<sup>61</sup>. “Force majeure” can be any unpredictable situation that is beyond the control of the party and which cannot be avoided notwithstanding any measure of due care and prudence exercised by this party. Occasions commonly referred to as “force majeure events” are

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<sup>58</sup> UNIDROIT/FAO/IFAD, Legal Guide on Contract Farming, 2015, p. 32

<sup>59</sup> In common law jurisdictions there is no general doctrine of force majeure, Ewan McKendrick, Force Majeure and Frustration of Contract, 1995, p.7

<sup>60</sup> Ibid, Ewan McKendrick, Force Majeure and Frustration of Contract, 1995, p. 11

<sup>61</sup> Art. 79 of the CISG does not use precisely the expression “force majeure” but it refers to “an impediment beyond a party’s control, Christoph Brunner, Force Majeure and Hardship Under General Contract Principles: Exemption for non- performance in international arbitration, Wolters Kluwer, 2009, p.17

war, strikes, riots, civil unrest, natural disaster such as hurricane, earthquake, drought, storms, floods etc<sup>62</sup>.

In contractual relationships built in the context of contract farming the concept of force majeure is of particular importance. Therefore, a provision in the contract that deals with force majeure issues and indicates the legal effects thereof is a key provision that offers legal certainty and renders the agricultural production contract thorough and comprehensive. It is commonly known that agricultural products are especially vulnerable and unforeseeable events - particularly those related to climatic change - may impair their quality or even the whole production. The big heat wave that plagued Western Europe in the summer of 2003, the outbreak of fires that hit almost all countries of South Europe (France, Spain, Portugal) in 2007, as well as heavy rainfalls that England experienced during the same time-period had an adverse effect on agricultural production in all this geographic area<sup>63</sup>. Furthermore, other sudden events such as crop or livestock diseases, epidemics and pest-attacks are frequent risks that can seriously harm agricultural production and hence thwart contract's equilibrium. Apart from these occasions there are several other circumstances that might affect the contractual relations of an agricultural production contract and are related to political or governmental decisions. Characteristic cases are commercial embargos, changes of laws and regulations that govern the contract, ban of exports, strikes and riots, depreciation of currency or capital controls<sup>64</sup>. The aforementioned factors constitute major obstacles to the performance of agricultural production contracts.

In light of the above it is evident that dealing with force majeure events is an overarching issue in contract farming constellations. As indicated previously, an unpredictable event qualified as force majeure event might disturb the balance of the contract and might render the obligations of one party onerous and cumbersome. In such situations clear-cut provisions that describe which party bears the risk of non performing obligations as a result of a force majeure event would be essential. Hence, it becomes apparent that the notion of force majeure is closely related to risk allocation

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<sup>62</sup> Caterina Pultrone with contributions from Carlos da Silva and Carmen Boulon Caro, Legal Fundamentals for the design of contract farming agreements, FAO, p. 2

<sup>63</sup> Bank of Greece climatic change, <http://www.bankofgreece.gr/BoGDocuments.pdf>

<sup>64</sup> UNIDROIT/FAO/IFAD, Legal Guide on Contract Farming, 2015, p.127

and risk mitigation issues<sup>65</sup>. Nonetheless, risk allocation is not an easy task; it requires clarity of intentions of contracting parties, ability to identify and assess the risks and most significantly expert advisors to design and draft suitable clauses that provide fairness and legal certainty and safeguard the equilibrium of the contract.

Most of the legal systems that recognize the legal notion of force majeure – usually under the domestic provisions of contract law or law of obligations – acknowledge as legal consequence that force majeure is a legitimate cause for the excuse of contract non-performance<sup>66</sup>. In other words the occurrence of an unpredictable event, which is qualified as a force majeure situation, entails the relief of the non-performing party from its duties and obligations set out in the contract<sup>67</sup>. Accordingly, the failure to fulfill contractual obligations due to force majeure does not establish liability for damages and hence the other party is not entitled to claim damages for breach of the contract<sup>68</sup>.

Taking into account that natural calamities are inherent in agricultural production contracts and also that there is high degree of interdependency among the obligations of the parties it can be perceived that the legal effects of force majeure, as described above, can be determinative for the balance of the contract. Therefore, not stipulating force majeure issues in the contract is not advisable, for it might precipitate undesired consequences. In contrast, allocating and/or mitigating the risk through carefully drafted stipulations tailored to meet parties' expectations are considered a fair and equitable solution. In practice, the risk resulting from force majeure events can be allocated or mitigated through contractual stipulations that provide for various remedies targeting at restituting the balance of the contract. By way of example, they may provide the possibility of the parties to terminate the contract or to renegotiate the terms and conditions thereof, to agree on certain agricultural insurance schemes, to continue the contract after a suspension period, when the force majeure situation will cede to exist, to agree on a minimum amount of compensation for losses or to have the right to fully

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<sup>65</sup> Ibid, Unidroit Legal Guide on Contract Farming, 2015, p. 129

<sup>66</sup> Tiphaine Guelou, Contract Farming and Force majeure- A review of clauses in contracts, Unidroit Working Group for the preparation of a Legal Guide on Contract farming, 2012

<sup>67</sup> Same approach is provided by Art. 7.1.7 of the Unidroit Principles of International Commercial Contracts (2010)

<sup>68</sup> UNIDROIT/FAO/IFAD, Legal Guide on Contract Farming, 2015, p. 188

or partially recover the damages<sup>69</sup>. Obviously, within the context of freedom of contracts the parties are able to negotiate and ultimately to agree freely on these and other terms and conditions that suit their needs. However, regard should always be had to the applicable law, which is not irrelevant even when parties exercise their right to contract freely, because the applicable law might regulate the issue of force majeure differently and might provide for mandatory rules from which the parties cannot derogate<sup>70</sup>.

One last remark that is worth noting touches upon the matter of distinction of the notions “force majeure” and “change of circumstances”<sup>71</sup> which is very subtle and can trigger disputes among the parties if confused. “Change of circumstances” is a similar legal notion that has many common elements compared to force majeure. It is described as the situation where the performance of the contract becomes excessively onerous or difficult for one of the parties due to unforeseen circumstances after the conclusion of that contract<sup>72</sup>. The core difference between the two notions is the legal consequence that each entails: whereas force majeure constitutes a legitimate cause for the exemption of liability for non-performance, in change of circumstances the performing party affected by this change usually is not exempted from its duty to perform, no matter if performance has become difficult or onerous, and may employ other remedies to recover the balance of the contract<sup>73</sup>.

It follows from the foregoing that the two notions are distinct and the one does not necessarily encompass the other. Consequently, the contract should contain express provisions for each situation, determining respectively the legal consequences. The silence of the agricultural production contract over the different legal treatment of the circumstances that fall within the notions of “force majeure” and “change of

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<sup>69</sup> Unidroit Secretariat, Unidroit Working Group for the preparation of a Legal Guide on Contract farming, 2013, A preliminary outline of issues, p.37

<sup>70</sup> UNIDROIT/FAO/IFAD, Legal Guide on Contract Farming, 2015, p. 130

<sup>71</sup> In international contracts and in literature is also encountered the term “hardship” to describe an exceptional change of circumstances that may give rise to a contractual remedy, Ibid, Legal Guide on Contract Farming, 2015, p. 128

<sup>72</sup>Rodrigo Momberg Uribe, Change of circumstances in international instruments of contract law. The approach of the CISG, PICC, PECL AND DCFR, <http://www.cisg.law.pace.edu/cisg/biblio/uribe.pdf>

<sup>73</sup> UNIDROIT/FAO/IFAD, Legal Guide on Contract Farming, 2015, p. 128

circumstances”, may lead to disputes and ultimately the judge is the one who will interpret the will of the parties and will order the legal effects according to the applicable law, solution which might essentially deviate from what the parties had anticipated.

## **2.5 Enforcement mechanisms in agricultural production contracts**

Concluding the illustration of some of the most interesting issues that arise during the life cycle of an agricultural production contract particular reference should be made to the enforcement stage, which presents a few core points that merit discussion.

It is apparent that when signing a contract a set of obligations is established for all contracting parties, which in case of breach create enforceable rights for the aggrieved party. On the other hand it is almost natural that the contract, at some point of its life-cycle, will produce controversies, disagreements or disputes. This may also be the case for agricultural production contracts, for, as explained, the nature of this contract is complex and entails some difficulties in the legal treatment of various issues, especially when those issues remain unregulated and are not dealt with in the contract<sup>74</sup>. It also holds truth that a badly designed and quick-drafted farming contract may aggravate a possible disagreement. For this reason the provision of suitable enforcement mechanisms is equally important and definitely can offer outlets, when parties feel legally entangled.

Analysis of “termination clauses”, which also considered enforcement mechanisms<sup>75</sup>, in the sense that they impose a “threat” for the occasion of non performance<sup>76</sup>, escapes the target of this paper. Certainly, special provisions as regards the grounds on which a party can terminate the agricultural production contract may help parties realize better their obligations and can give rise to enforcement procedures. However, parties should be aware of what termination actions entail and be able to assess the costs and benefits of breaking the contract. A rush recourse to termination

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<sup>74</sup> Ibid, Legal Guide on Contract Farming, 2015, p. 204

<sup>75</sup> Marta Doria with contribution of Carlos da Silva, Contract Farming: Legal Considerations on contractual design and enforcement, FAO, [http://www.fao.org/fileadmin/user\\_upload/contract\\_farming/Brief%201%20legal%20aspects%20of%20contract%20farming.pdf](http://www.fao.org/fileadmin/user_upload/contract_farming/Brief%201%20legal%20aspects%20of%20contract%20farming.pdf)

<sup>76</sup> UNIDROIT/FAO/IFAD, Legal Guide on Contract Farming, 2015, p. 220

may thwart the contractual relations leaving all parties with casualties, be it financial loss or damaged business reputation.

Thorough provision of dispute resolution clauses generally serves as adequate enforcement mechanism and can add value to an agricultural production contract enhancing contract's efficiency, encouraging mutual trust among the parties and forwarding legal certainty. Thus, a well-drafted dispute resolution clause is of particular importance. Most often dispute resolution clauses opt for the Court system, which is a widely accepted and trustworthy enforcement mechanism in almost all legal systems. Nevertheless, some shortcomings of the judicial system that are reported at various jurisdictions have given fresh impetus for the development of alternative dispute resolution mechanisms. Notwithstanding that arbitration has long been established as an effective alternative dispute resolution method, recently other modern alternative dispute resolution mechanisms have been developed gaining ground constantly.

It is argued that a contract clause which, in case of a dispute, provides for a negotiation process and subsequently, if negotiations fail, mediation<sup>77</sup> or arbitration serves best the agricultural production contract<sup>78</sup>. This option is further encouraged due to the extremely slow litigation procedures from which many legal systems suffer and unfortunately this fact has adverse effects in many business ventures, including contract farming arrangements<sup>79</sup>.

Through negotiation parties might find legal solution inspired by principles such as mutual trust, cooperation and equity. The role of third persons is important, as they can assist contributing to the resolution of the dispute and offering advisory, technical or coordination services to the parties. As obvious, negotiation process is a way of amicable dispute resolution and can be coupled with conciliation or mediation, which also target at the same end. In general, these amicable ways of dispute resolution present many advantages: they are much less costly than litigation and arbitration, they are fast, parties can proactively involve in the procedure expressing their opinion and

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<sup>77</sup>Caterina Pultrone with contributions from Carlos da Silva and Carmen Boulon Caro, *Legal Fundamentals for the design of contract farming agreements*, FAO, p. 4

<sup>78</sup> UNIDROIT/FAO/IFAD, *Legal Guide on Contract Farming*, 2015, p. 205

<sup>79</sup> IFAD, "Egypt: Smallholder contract farming for high value and organic agricultural exports"  
<https://www.ifad.org/documents/10180/0d1e3f6c-450b-4b67-92b2-5d23b2f9f4f0>

ultimately a possible settlement is much more likely to be implemented and enforced, as it is the outcome of parties own will<sup>80</sup>.

Arbitration, be it a stand-alone clause that provides for the settlement of disputes or is combined with negotiation or mediation is acknowledged as an effective method of dispute resolution that above all guarantees enforceability. Arbitration is a familiar method especially in commercial cases and hence is strongly recommended for contract farming. The stronger advantage of arbitration is that, similar to a court decision, arbitral awards are binding and enforceable. Moreover, arbitration is quick, affordable, more simple as regards rules of evidence and procedure and most significantly arbitrators usually are experienced professionals with deep knowledge of commercial and business issues<sup>81</sup>. This last point is of great importance for contract farming arrangements, because, as earlier discussed, contract farming actually constitutes a business model in the sector of supply chain that presents particularities and thus requires experience and expert knowledge.

Notwithstanding the plethora of advantages that usually alternative dispute resolution methods have, that is not to say, that the agricultural production contract is inoperative or ineffective, if contains a traditional dispute resolution clause, whereby future disputes will be resolved through litigation in Courts. Both systems can guarantee enforceability and can offer legal certainty and effectiveness, as long as the contract encompasses clear-cut and well drafted provisions with a view to protect parties' interests, to establish mutual trust among the parties and ultimately to promote the viability of agricultural production contracts. A useful, though recurrent observation: parties should always take into consideration the applicable law and possible mandatory rules, in order to enforce their rights successfully.

### **CHAPTER 3**

#### **CRITICAL ISSUES FOR SUSTAINABLE CONTRACT FARMING ARRANGEMENTS**

##### **3.1 PREFACE**

The previous chapter examined some basic legal aspects that stem from the implementation of agricultural production contracts, whose proper legal treatment can

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<sup>80</sup> UNIDROIT/FAO/IFAD, Legal Guide on Contract Farming, 2015, p. 210-211

<sup>81</sup> UNIDRO IT/FAO/IFAD, The Legal Dimension of Contract Farming, Bangkok, September 2014, p.17

promote contract farming and can lead to efficient legal arrangements. In line with what has already been discussed, this chapter aspires to illustrate a few critical issues that do not purely fall within the field of contract farming but, if combined, can form enabling environment for the latter and give fresh impetus to successful and profitable contract farming agreements.

Hence, the following paragraph of the present chapter examines the issue of public private partnerships and how this initiative can contribute to contract farming operations. Paragraph 3.3 deals with the role of insurance schemes in agricultural production contracts and assess how insurance can impact on parties' relations, whereas the last paragraph touches upon the interesting issue of financing of contract farming ventures and explores the available financial tools and other mechanisms that exist or can be designed, in view to promote contract farming and to ensure its financial viability.

### **3.2 Public private partnerships and contract farming**

The term Public Private Partnerships (PPPs) can be described as the form of cooperation between public authorities and economic operators<sup>82</sup> that aims at the implementation of high-value development projects in the field of works or services, such as transport infrastructure, constructions, electricity, communication systems, waste management and other environmental services, national security services, public health services, namely projects that traditionally are provided by the public sector. The rationale of this initiative lies in the fact that public sector, despite the growing demand for development, has rather limited fund availability for investments and also its potential for pooling funds from other sources is rather narrow. Besides, the recent global financial crisis, which has been transformed into a sovereign debt crisis, has dramatically affected the funding conditions for governments<sup>83</sup> and thus their ability to provide services of public interest has become all the more cumbersome.

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<sup>82</sup> Green Paper on public-private partnerships, <http://eur-lex.europa.eu/legal-content/EN/TXT/HTML/?uri=URISERV:l22012&from=EN>

<sup>83</sup> Andreas Dombret: Europe's sovereign debt crisis – causes and possible solutions. Speech by Dr Andreas Dombret, Member of the Executive Board of the Deutsche Bundesbank, to the Deutsche Alumni, Frankfurt am Main, 20 December 2011, <http://www.bis.org/review/r120111b.pdf>.

Partnership between the public and the private sector has proved to be an effective method for financing public investments<sup>84</sup>, as governments can materialize their target for development without spending money from the national budget, being instead financed by the private sector. As acknowledged<sup>85</sup>, private sector has greater potential to raise funds from the markets, is better organized than the public sector and has the comparative advantage that possesses the necessary know-how for large scale projects and also enjoys better information and project technology access. These factors are conducive to the effectiveness of PPP projects, which gain ground worldwide as an alternative means of financing public investments.

In parallel, the development of the agricultural sector is of high priority for many national economies, as it is evidenced that it can contribute decisively to the national budget and consequently to economic growth. Many governments being aware of the potential of agriculture undertake various initiatives to further promote and foster their national agricultural sector. Contract farming is undoubtedly a business method that can empower agricultural economy and so it is natural to draw the interest of the public sector. The dissemination of the concept of PPP and its wide success in other fields of economy, coupled with the weakness of the public sector, as described above, to be engaged in large scale investments, has urged governments to strongly support the implementation of PPP projects also in the field of agriculture and particularly in contract farming arrangements as a useful tool to attract private investors in response to the need for promotion of agricultural development<sup>86</sup>.

The implementation of PPP projects within the framework of contract farming can be associated with various objectives and fields of activities depending on the needs that a government intends to cover. More particularly, predominant role in contract farming plays the existence of adequate infrastructure which is absolutely indispensable for the promotion and the effectiveness of this specific supply chain business model. Poor rural roads, limited or extremely expensive electric power, inadequate irrigation

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<sup>84</sup> For the historical context of PPP see the Overview of PPP experience, <https://ppiaf.org/sites/ppiaf.org/files/documents/toolkits/highwaystoolkit/6/pdf-version/1-21.pdf>

<sup>85</sup> Jeffrey Delmon, *Private Sector Investment in Infrastructure*, second edition, Kluwer Law International, p. 16

<sup>86</sup> UNIDROIT/FAO/IFAD, *Legal Guide on Contract Farming*, 2015, p. 6

systems or insufficient water storage infrastructure may affect contract farming arrangements, in the sense that they may serve as disincentives for possible investments or may establish an uncompetitive environment<sup>87</sup>. Hence, PPP projects that target at restructuring utilities or constructing roads and basic infrastructure works are very common in contract farming arrangements.

Moreover, there are cases where PPP projects are agreed, in order land issues to be addressed. In agricultural production contracts most probably the producer owns the land where the production will take place. However, it is not uncommon the situation where the State owns land and participates in a PPP project, through which the State allocates the land to a specific producer or an association of producers, concluding with them pertinent lease contracts, facilitating them this way to engage in contract farming arrangements<sup>88</sup>.

An interesting target very often pursued by public partners in PPP projects implemented in the framework of contract farming schemes, relates to the issue of capacity development, especially as regards small-scale producers. Central governments and regional authorities are well-aware that capacity building can offer to smallholder farmers the necessary dynamics to participate in contract farming arrangements in equal terms, boosting this way their income and stimulating the agricultural sector, as well as national economy in total. Instilling technical knowledge into farmers, transferring technology and useful information, as regards production/harvesting methods, crops varieties, agricultural marketing and other similar information, can lead to increased farm productivity, can reduce unit production costs and overall can contribute to sustainable contract farming schemes, while on the other hand individual farmers can take advantage of economies of scale and can compete in a global marketing environment<sup>89</sup>. Food security, poverty reduction, environmental protection are also key- objectives that motivate public sector to participate in PPP initiatives, in an effort to rationalize the agricultural sector and to promote contract farming as an innovative and effective business model in agribusiness.

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<sup>87</sup> Government of Kenya, Agricultural Sector Development Strategy 2009-2020 p. 33

<sup>88</sup> UNIDROIT/FAO/IFAD, Legal Guide on Contract Farming, 2015, p. 96

<sup>89</sup> Government of Kenya, Agricultural Sector Development Strategy 2009-2020 p. 64

A few real paradigms of PPP projects that have been implemented or are currently implemented worldwide within the framework of contract farming arrangements will further illustrate the importance of the concept of public private partnerships (PPP) for the agricultural sector and for contract farming in general<sup>90</sup>. More particularly, the Ghana Rubber is a partnership between the Agricultural Development Bank of Ghana and AFD of France (a public industrial and commercial institution), whose purpose is to rehabilitate the distressed rubber estates that used to be a traditional source of export commodity for Ghana. The objectives of the agribusiness investment are to, among others, cultivate 50.000 hectares of rubber by 2020 and rehabilitate the road infrastructure in various districts of Ghana<sup>91</sup>. In Indonesia an ongoing PPP project among public entities and various farmer groups motivate, train and coach 10,000 farmers, using certified rice seeds and organic fertilizers and pesticides. The objective for the public sector is notably food security, whereas the incentives for farmers are price stability, market access and technical assistance<sup>92</sup>. The Southern Agricultural Growth Corridor of Tanzania (SAGCOT) is a PPP scheme in which farmers, agri-businesses, the Government of Tanzania and companies from across the private sector participate aiming at fostering agribusinesses, improving food security and reducing rural poverty<sup>93</sup>. PYMERURAL is a program of public private interaction for the competitive development of agribusinesses in Honduras and Nicaragua. In the framework of this program public and private entities collaborated to improve financing mechanisms for cacao producers in Honduras and to improve infrastructure for better drying and fermenting practices<sup>94</sup>.

This brief review of these characteristic case studies of agri-PPP projects reveals that PPP initiatives appeal to both private and public sector, for predominantly serve the mutual interests of the parties. Offering potential to leverage financing, sharing the risk in doing business in the agricultural sector, providing market access to small-scale

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<sup>90</sup> For more PPP projects visit <https://www.ifad.org/documents/10180/451226eb-1fc6-4474-b39d-f3cafed5164a>

<sup>91</sup> <http://www.fao.org/docrep/017/aq231e/aq231e.pdf>

<sup>92</sup> FAO, Public Private Partnerships for agribusiness development, 2016, p. 57-58

<sup>93</sup> <http://www.sagcot.com/>

<sup>94</sup> Ingrid Fromm, Linking small scale cacao farmers from Honduras to the Swiss Chocolate Industry through targeted partnerships, <https://mfe.be/choconomics/fromm.pdf>

farmers are only some of the benefits of agri- PPP projects<sup>95</sup>, which can transform agricultural sector into a backbone of national economies. To the extent that public-private partnerships can encourage investments in agricultural value chain demonstrates that PPP schemes are a useful method for promoting contract farming as well. Indeed, PPP projects contribute substantially to successful contract farming arrangements, as ultimately synergies in the agricultural sector enable sustainable growth and enhance smallholder productivity and livelihoods<sup>96</sup>, whereas at the same time they boost product quality; all these are common objectives that contract farming constantly pursues.

### **3.3 Agricultural insurance as a risk management tool in contract farming**

In para.2.2 is noted that insurance is a form of risk management, through which a person or an entity seeks protection from the insurer against future potential losses in exchange for a premium, namely a certain amount of money paid by the insured for specific risks coverage. At the same time insurance is a financial service, in the sense that, in fact, it provides financial assistance to the insured persons, which selecting the proper insurance product envisage to mitigate the economic consequences derived from the occurrence of the insured risks.

Risk in agriculture is a pivotal issue. Beyond any doubt farming activities are closely associated with various risks and difficulties that may destabilize the farm venture and may frustrate farmers' expectations. Pests and diseases, fires, extreme weather conditions like storms, hurricanes, floods, drought and also wild-animals attacks are very common risks that farmers face and might lead to yield losses. Another category of risks is related to post-harvest losses possibly due to unsuitable storage or transport conditions of the agricultural production, whereas price fluctuations on markets and other similar extraordinary events pose significant risks and ultimately increase the level of uncertainty for the farmers<sup>97</sup>. These risks are crucial even for large-scale producers in

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<sup>95</sup> FAO, Public Private Partnerships for agribusiness development, 2016, p. 6-7

<sup>96</sup> Marco Ferroni, Paul Castle, Public- private partnerships and sustainable agricultural development, 2011, file:///C:/Users/ACER/Downloads/sustainability-03-01064.pdf

<sup>97</sup> Silvia Müller, Gaby Ramm and Roland Steinmann, Agriculture, Microinsurance and Rural Development, 2014, p. 7

[http://www.microinsurancenetwerk.org/sites/default/files/MICRO\\_Network-Brochure\\_agriculture%20rural-2-WEB.pdf](http://www.microinsurancenetwerk.org/sites/default/files/MICRO_Network-Brochure_agriculture%20rural-2-WEB.pdf)

developed countries, but positively are much more determinative for smallholder farmers, who more than anyone else need protection, targeted interventions and relief measures<sup>98</sup>.

In response to this need the sector of agricultural insurance has become increasingly popular and evolves constantly offering suitable and well-designed insurance products intended to meet the demands of all interested parties engaged in the realm of agriculture. Targeting at covering all possible farmers' needs for insurance insurers have developed various programs offering this way a holistic protection of the agricultural production. Consequently, a full agricultural insurance package can contain insurance of agricultural premises, installations and buildings, of agricultural vehicles and machineries, insurance of production's transportation, crop and livestock insurance and also insurance for third-party liability coverage. These are typical risks covered by the insurers, but each insurance company can develop its own agricultural insurance policies depending on the country where it operates and the specific needs of the agricultural sector in a particular area.

A study of the European Commission on Agricultural Insurance Schemes lists the types of insurance in agricultural sector, in terms of the risks covered, and reports on the various agricultural insurance schemes that exist worldwide. According to this study the single-risk insurance scheme covers mostly one risk or two similar risks (e.g. hail or hail and fire), the combined insurance scheme covers a combination of risks, whereas the yield insurance scheme covers all risks that affect the production. Furthermore, there is the price-insurance scheme that covers a certain amount of production against price fluctuations, the revenue insurance scheme, which combines yield and price risk coverage in one insurance product. The latter scheme is considered more expensive, but more efficient as income stabilizer. Moreover, the whole-farm insurance scheme provides for a combination of guarantees for various farm products on the same farm, whereas through the income insurance scheme yield and price risks are covered as well as the costs of production. A very familiar insurance scheme is the index insurance that is based on an index, such as rainfall, temperature, humidity, wind speed, crop yields or

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<sup>98</sup> Ulrich Hess, Peter Hazell, Innovations and Emerging trends in Agricultural Insurance, GIZ 2016, p. 7

livestock mortality rates, rather than actual economic losses; it is generally a cheaper scheme and easier to manage and control, but its disadvantage is that it is not linked to the farmers income. The same study of the EC reports that the EU has mostly classic insurance schemes (mainly single-risk and combined insurance, but also yield insurance), whereas in the USA, Canada and other non-EU Countries most familiar are other insurance schemes, such as index insurances, whole- farm insurance or revenue insurance<sup>99</sup>.

In agricultural production contracts the value of insurance is all the more important due to the particularities and the special characteristics that the concept of contract farming encompasses. First and foremost, the fact that parties are bound with a contract makes their obligations even more burdensome and thus parties are most interested in risks management issues, in order to avoid mishaps and be able to fulfill their contractual obligations more smoothly. Farmers engaged in contract farming arrangements are especially burdened with increased obligations primarily because most often contractors set their own production conditions, in terms of crop quality and crop quantity, technical or timing specifications, and producers must strictly comply with these requirements in conformity with the express terms and conditions of the contract. Hence, agricultural insurance for farmers is a core subject and is frequently encountered in many agricultural production contracts serving as a valuable tool for contractual risks management.

As explained in para 2.4, crop or livestock diseases, epidemics and pest-attacks, as well as unforeseeable weather conditions are qualified as force majeure issues and are frequent risks within the context of agricultural production contracts that threaten the production process. Consequently, insurance schemes that are most common in contract farming arrangements are those that provide coverage for crop damages<sup>100</sup>. Of course, depending on certain obligations that the producer expressly agrees with the contractor (e.g. obligation to storage contractor's inputs, to take care of the inputs or to

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<sup>99</sup> Maria Bielza, Costanza Conte, Christoph Dittmann, Javier Gallego, Josef Stroblmair, European Commission Final Report, 2006 modified in 2008, Agricultural Insurance Schemes, Administrative Arrangement N °.AGRI-2005-0321 between DG Agriculture (DG agri) and DG joint research centre p. 15, 32

<sup>100</sup> Doug O' Brien, Neil Hamilton, Robert Luedeman, The farmer's legal guide to Producer Marketing Association, 2005, The National Agricultural Law Center, University of Arkansas p.67

make exclusive use thereof only for purposes of the contract)<sup>101</sup> or depending on the type of the agricultural production contract, farmers may be obliged to obtain insurance for various other risks that relate to these specific obligations, particularly in cases where these obligations appear to play a predominant role for the parties' interest and are crucial for the balance of the contract<sup>102</sup>. Respectively, agricultural insurance may also attract contractors' interest as well. This may be the case when contractors are liable for the livestock, and thus liability and casualty insurance on the livestock is required. Furthermore, contractors may have tort liability towards third parties and in this case purchasing the proper insurance program would be highly advisable<sup>103</sup>. It is worth noting that in some cases producers, especially at the outset of the contractual relationship when the uncertainty for the outcome is more intense, might be reluctant to purchase insurance; in such circumstances contractors may be able to provide insurance deducting premiums for repayment at harvest time, making this way insurance affordable for farmers<sup>104</sup>. In this sense it is apparent that insurance promotes contract farming arrangements and facilitates the contractual relations among the parties.

From the above mentioned it can be perceived that insurance plays a major role as mechanism of risk mitigation in agricultural production contracts<sup>105</sup>. The practice has shown that insurance schemes tailored to the needs of the parties in contract farming arrangements can share the commercial risk of the venture and can serve as a safety net in cases of contract default<sup>106</sup>. Insurance empowers especially the smallholder producers by transferring natural risks out of the context of the agricultural production,

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<sup>101</sup> UNIDROIT/FAO/IFAD, Legal Guide on Contract Farming, 2015, p. 93

<sup>102</sup> Useful remark: the producers can have insurable interest and are entitled to compensation from insurance companies for crop damages even if they don't have legal title to the crops, *ad hoc Parks v. Federal Crop Insurance Corporation FCIC* 416 F 2d 833 7 CA 1969, Neil Hamilton, *Farmer's Legal Guide to Production Contracts*, 1995, The National Agricultural Law Center, University of Arkansas, p.86

<sup>103</sup> UNIDROIT/FAO/IFAD, Legal Guide on Contract Farming, 2015, p. 98

<sup>104</sup> Lorenzo Casaburi, Michael Kremer, Alphonse Odondo, John Shoven, *Tailoring Contract Farming to Smallholders: Experimental Evidence on Enrollment Impact, Insurance Provision, and Communication Technologies*, p.4, [http://basis.ucdavis.edu/wp-content/uploads/2013/12/Shoven\\_Proposal.pdf](http://basis.ucdavis.edu/wp-content/uploads/2013/12/Shoven_Proposal.pdf)

<sup>105</sup> Caterina Pultrone, Carlos Da Silva, Andrew Sepherd, *Guiding Principles for responsible contract farming operations*, FAO 2012, P. 4

<sup>106</sup> UNIDROIT/FAO/IFAD, Legal Guide on Contract Farming, 2015, p. 30

hence protecting farmers' livelihoods and enhancing their creditworthiness towards contractors<sup>107</sup>; furthermore, it facilitates their access to means of production and overall reduces income uncertainty<sup>108</sup>.

Concluding and adding some more positives to the importance of insurance for contract farming, it can be argued that it is an effective tool for risk management in contract farming arrangements, especially if compared to other alternative tools. As competitive advantages could be cited that farmers have a direct legal title to claim their compensation and also that farmers engaging in insurance contracts acquire all necessary information and knowledge, very helpful to take rationale decisions and be more realistic with the management of the contract. Overall, the role of insurance in contract farming is catalytic, as ultimately contributes to successful relationships and improves the economic sustainability of agricultural production contracts<sup>109</sup>.

### **3.4 Financing mechanisms of contract farming**

In every business venture financing is essential component for its start up process, its organization and operation, as well as its further development<sup>110</sup>. Sustainability of a business depends to a great extent on the existence of capital flows that enable entrepreneurs to manage the business, to take advantage of opportunities (commercial or investment) and ultimately to inject money into the overall economy. Notwithstanding its importance, access to financing is not an easy task and puzzles especially small and medium sized business owners. The situation is more complex as regards the financing of the agricultural sector; the majority of smallholder farmers and micro agribusinesses can hardly meet the criteria and conditions that commercial banks and financial institutions often set, in order to furnish funds, loans and other financing

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<sup>107</sup> Ulrich Hess, Peter Hazell, Innovations and Emerging trends in Agricultural Insurance, GIZ 2016, p. 1

<sup>108</sup> Silvia Müller, Gaby Ramm and Roland Steinmann, Agriculture, Microinsurance and Rural Development, 2014, p. 37-39

<sup>109</sup> Maria Bielza, Costanza Conte, Christoph Dittmann, Javier Gallego, Josef Stroblmair, European Commission Final Report, 2006 modified in 2008, Agricultural Insurance Schemes, Administrative Arrangement N °.AGRI-2005-0321 between DG Agriculture (DG agri) and DG joint research centre p. 188-189

<sup>110</sup> Doug O' Brien, Neil Hamilton, Robert Luedeman, The farmer's legal guide to Producer Marketing Association, 2005, The National Agricultural Law Center, University of Arkansas p . 47

tools<sup>111</sup>. This has been a recurrent problem and has proved to be a major impediment for the financially weaker actors of the agricultural sector, predominantly in developing, but also in developed economies as well, which subsequently has led them to marginalization or to subsistence at best.

The improvement of rural livelihoods and incomes, as well as food security issues and rationalization of agricultural supply chain were always high in the agenda of the policies of agricultural sector. These policies to a great extent have been achieved through the development of the concept of contract farming. The overarching strong points of contract farming have already been mentioned<sup>112</sup>; the following lines are dedicated to a more detailed analysis of the financial facet of contract farming and notably of its contribution as a facilitator for access to financing.

Undoubtedly, one of the most significant advantages of contract farming is that it provides better financing opportunities to the parties of the contractual arrangement<sup>113</sup>. Producers and contractors, namely agribusinesses or supply chain trade companies, can have access to credits and be financed by credit/financial institutions using the agricultural production contract as collateral. It is common knowledge that banks offer loans, if the latter are backed by assets of almost equal value owned by the borrower, as collateral. This practice has been for years an insurmountable obstacle for farmers and entrepreneurs that simply lacked assets and hence were excluded from financing. The concept of contract farming meets worldwide wide acceptance for, above all: succeeds to establish robust and long-term relationships among the basic participants of the value chain, based on mutual interest; creates legal certainty achieved by express and clear contractual terms of common understanding agreed by experienced stakeholders of the agricultural sector; furthermore it produces economies of scale, which could be of great benefit for national economies, as well. All these features add value to contract farming arrangements and give a new dynamics to this innovative business model,

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<sup>111</sup> Other factors that conduce to limited financing is the inability of farmers to offer collaterals to banks in order to release credits, their limited knowledge of finance and business management, the inherent risks and instability of agricultural production, government interventions in the agricultural sector, Reuben Jessop, Boubacar Diallo, Marjan Duursma, Abdallah Mallek, Job Harms, Bert van Manen, *Creating Access to Agricultural Finance*, 2012, AFD A' Savoir 14, p. 25-33

<sup>112</sup> See para 1.2

<sup>113</sup> UNIDROIT/FAO/IFAD, *Legal Guide on Contract Farming*, 2015, p. 4,7

which is dealt by most market operators as a reliable and viable business instrument within the agricultural supply chain<sup>114</sup>. Likewise, banks and other credit and financial institutions acknowledge that contract farming can be a profitable business scheme which presents fewer credit risks than other commercial ventures<sup>115</sup> and thus are more willing to offer loans to the parties, as practically they secure their credits through the anticipated sale of the agricultural production in the future.

Apart from this direct financing through the banks, access to financing can also be indirect through the contractors, who can also provide or facilitate credits to the farmers<sup>116</sup>. Producers, at the outset of an agricultural production contract, encounter increased production costs, namely expenses for seeds, fertilizers, pesticides, packaging materials, energy etc. Contractors can provide financial assistance undertaking to cover all these costs, whereas the repayment of this kind of credit can be deducted from the value of the end production<sup>117</sup>. It is evident that in this case of indirect financing again the agricultural production contract serves as a kind of collateral that guarantees the credit, as in essence the contractor underpins its confidence on the implementation of the agricultural production contract, concluded with the certain producer to which he has provided the credits, and more particular on the dynamics of the value of the future production<sup>118</sup>.

It follows from the foregoing that contract farming has been established as an alternative financing mechanism in the agricultural sector<sup>119</sup> which has gained the confidence of the markets and has enabled the financially weaker operators within the agricultural value chain to have access to finance guaranteeing liquidity to them. This in turn has created a new reality for small farmers and agribusiness which, through the

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<sup>114</sup> Ayelech Tiruwha Melese, *Contract Farming: Business Models that Maximise the Inclusion of and Benefits for Smallholder Farmers in the Value Chain*, Rev. dr. unif. 2012, p. 291

<sup>115</sup> Reuben Jessop, Boubacar Diallo, Marjan Duursma, Abdallah Mallek, Job Harms, Bert van Manen, *Creating Access to Agricultural Finance*, 2012, AFD, A' Savoir 14, p. 47-51

<sup>116</sup> Ibid, p. 44

<sup>117</sup> Ibid, p. 47

<sup>118</sup> Relevant is footnote 103 as regards insurance provided by the contractor as a form of financial assistance to the producer.

<sup>119</sup> Moses Moyo, *Effectiveness of a Contract Farming Arrangement: a case study of tobacco farmers in Mazowe district in Zimbabwe*, 2014, [http://www.fao.org/uploads/media/moyo\\_effectiveness\\_%20%202014.pdf](http://www.fao.org/uploads/media/moyo_effectiveness_%20%202014.pdf)

modernization of agriculture, can experience development, new perspectives and better livelihoods.

In parallel, the acceleration of the agricultural sector and the rationalization of the agricultural supply chain, achieved to a great extent through contract farming arrangements, leverage the interest of various other traditional financial service providers within the agricultural sector, which seem to be attracted by this innovative business model and thus are motivated to design and implement further financing mechanisms to support contract farming arrangements. Microfinance institutions, rural banks and credit associations worldwide are typical financial providers that launch relevant financing instruments in the form of loans, bank accounts, credit cards, leasing programs etc, in an effort to strengthen the agricultural sector and to facilitate profitable and viable agricultural ventures<sup>120</sup>.

In the same direction the public sector also serves as financial provider and is frequently engaged in the implementation of financing projects, in order to foster and promote agricultural activities<sup>121</sup>. Depending on the dynamics of the agricultural sector in each economy, governments can launch various programs; such are indicatively agricultural loans offered by state-owned banks under favorable terms and conditions, grants aiming at fostering particular agricultural sub-sectors or promoting certain best practices in agriculture<sup>122</sup> and credit guarantees, which can be provided to banks and microfinance institutions in order to encourage them to finance the agricultural sector<sup>123</sup>.

Special reference should be made to Agricultural Development Funds, which constitute a widespread practice in many agricultural –oriented national economies. These Funds are initiatives that emanate either purely from the public sector or are joint efforts of the public and the private sector, or of international/non-government

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<sup>120</sup> Reuben Jessop, Boubacar Diallo, Marjan Duursma, Abdallah Mallek, Job Harms, Bert van Manen, *Creating Access to Agricultural Finance*, 2012, AFD, A' Savoir 14, p. 34

<sup>121</sup> Doug O' Brien, Neil Hamilton, Robert Luedeman, *The farmer's legal guide to Producer Marketing Association*, 2005, The National Agricultural Law Center, University of Arkansas p. 67

<sup>122</sup> *Ibid* p. 50

<sup>123</sup> Reuben Jessop, Boubacar Diallo, Marjan Duursma, Abdallah Mallek, Job Harms, Bert van Manen, *Creating Access to Agricultural Finance*, 2012, AFD, A' Savoir 14, p. 64

organizations<sup>124</sup> and are committed to financially supporting agriculture throughout the value chain, targeting primarily to increase the interest in investing in the agricultural sector<sup>125</sup>. Similar initiatives exist also at EU level, where the European Commission in cooperation with governments of developing countries can establish Development Funds<sup>126</sup>, which are actually financing agreements that provide for direct investments and granting schemes in agricultural projects implemented within the territory of the certain country.

In addition to the financing mechanisms that already have been mentioned, reference to the funding opportunities that offered by the EU could not be omitted. The EU, within the framework of the Common Agricultural Policy (CAP) has established two EU funds, the European Agricultural Guarantee Fund (EAGF) and the European Agricultural Fund for Rural Development (EAFRD). Under the EU Common Agricultural Policy (CAP), farmers can receive compensation for implementing certain policies and best practices that promote, inter alia, sustainable agriculture, food safety, and environmental issues. The policies and initiatives of those EU Funds are implemented in shared management between the Member States and the Union, which means that the EU does not proceed with direct payments to the beneficiaries of aid but this task is delegated to the Member States<sup>127</sup>. It is obvious that these funding opportunities are very relevant to contract farming arrangements and could boost further this business model; hence merit special attention.

## CONCLUSIONS

Without any doubt contract farming is an innovation in the agricultural sector, in so far as it manages to organize the agricultural production in a holistic manner, intervening from the stage of cropping and harvesting to storage, transport and marketing of the agri-products. At the same time it brings together various stakeholders that each one of them adds value to the project offering its expertise, while anticipating the relevant benefits. These synergies create a great potential and certainly contribute

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<sup>124</sup> Pari Baumann, Equity and Efficiency in Contract Farming Schemes: the experience of agricultural tree crops, 2000, Overseas Development Institute, p. 27

<https://www.odi.org/sites/odi.org.uk/files/odi-assets/publications-opinion-files/2730.pdf>

<sup>125</sup> Government of Kenya, Agricultural Sector Development Strategy 2009-2020 p. 140

<sup>126</sup> [http://eeas.europa.eu/archives/delegations/uganda/projects/overview/faq/index\\_en.htm](http://eeas.europa.eu/archives/delegations/uganda/projects/overview/faq/index_en.htm)

<sup>127</sup> [http://ec.europa.eu/agriculture/cap-funding/funding-opportunities\\_en](http://ec.europa.eu/agriculture/cap-funding/funding-opportunities_en)

significantly to the development and improvement of the agricultural supply chain, offering simultaneously plenty of advantages to all participants.

The present dissertation does not adopt the view that contract farming is a panacea or a one-way road for the development of the agricultural sector; on the contrary the previous analysis highlights certain legal and policy considerations, in order to indicate the complexity, as well as the particularities of this concept. As explained, contract farming arrangements require, above all, careful business planning and legal consideration and any negative impacts or deficiencies should not be underestimated. Nevertheless, it cannot be ignored that contract farming develops considerable dynamics and that evolves as a business model with great promise. To the aim of its further success and sustainability the establishment of an enabling environment can be determinative; adequate legal and regulatory framework, finance and risk mitigation mechanisms, system of checks and balances, as regards agri-food quality and food safety, are of great importance and can conduce to the creation of credible, profitable and long-term contract farming relations.

However, it can be submitted that the most significant enabling factor for the sustainability of contract farming and for the conclusion of sound and transparent agricultural production contracts is the trust and confidence that participants should place in contract farming arrangements, as well as the purity of their intentions. Entering this business model for distortive, manipulative, or opportunistic reasons condemns it to failure; approaching it through dogmatic and biased positions also cannot help. Contract farming and its legal vehicle, namely agricultural production contracts, need above all qualified, open-minded and well –informed stakeholders, in order to further sustain and grow.

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