

- b) Confirm everything in writing. If the grower agrees verbally on some point, a confirming letter stating the agreement should be sent to the owner. The letter will state the grower's interpretation of the agreement and allow the owner time to respond. A copy of the letter should be kept on file.
- c) Be cautious of projections or examples. Unless otherwise stated, they are only examples and not guarantees.
- d) Make sure issues that are important to the grower are stated clearly in the contract. This part of the evaluation is difficult because the grower is looking for what is not there. Typically, the owner drafts the contract and may overlook points that are important to the grower. For example, the grower may not want any pigs with tails because he has had problems with tail biting in the past. Such concerns need to be expressed early on and described in the contract.

2. There is no substitute for working with reputable people.

- a) Find out about the other party. Do they have an established record of being a good business partner? Ask for references and talk to people that have dealt with them before.
- b) A contract does not force parties to comply with the agreement. However, a contract gives either party an avenue to prosecute the other should they violate the contract. The time and expense of litigation is costly, and unless the contract specifically states that the losing party in the lawsuit must pay the winner's cost, each party pays his own legal expenses.
- c) Is there an arbitration clause in the contract? Such a clause removes any disputes from the court system. This approach makes sense when only a small number of animals are involved. Beware of who the arbitrators are and how they are chosen. One example would be for each party to choose one, and the two of them choose a third.

3. What is the length of contract?

- a) The length of contract is particularly important if the grower is required to make capital improvements before hogs are placed on the farm. If new facilities or equipment is required, the grower may want an agreement that is long enough to justify the investment, say ten years on facilities or three years on new feeders.
- b) The cost of depopulating the grower's farm, if required, should also be considered. It may be worthwhile for several years of contracting, but not for only one group.
- c) The stated length of the contract and the ending date should coincide with production of the hogs. Some contracts run for a set time (i.e., one year), while others are in force until one of the parties terminates it. However it is stated, it should not end while hogs are in the facility. For example, set the length at one year with no hogs placed later than two months before the end of the contract and that all hogs in the facility at the end of the contract are subject to the same contract until they are sold.

4. How and why may the contract be terminated?

- a) The contract should list the steps required to terminate the agreement. How much oral or written notice is required to cancel a contract? A farrowing contract may require a month or more notice, while two days may be sufficient for finishing hogs.
- b) What are valid reasons for termination? Typically, failure to follow good animal husbandry practices is grounds for termination. However, the individual passing judgment should be an objective observer, not the owner's field worker.
- c) Termination by removal of the hogs. Some contracts allow the owner to enter the facility and remove his/her hogs at any time. While it is essential that the owner be able to make quick marketing and management decisions to protect his/her investment, the grower may want to be

assured of compensation if the hogs are removed before the end of the contract.

5. Delivery of owner's hogs.

- a) The grower may bear the cost of the owner's decision when to place hogs. While the grower may want to wait a few days for market conditions to improve before buying pigs, the grower with an empty facility pays the price of waiting. The grower may want to be compensated a certain amount of dollars per day that his/her building is idle beyond a specified number of days.
- b) In and out weights have an impact on the realized returns to the contract. Contracts paying a flat fee per head and/or feed efficiency bonuses are affected both by the starting weight and the amount of gain put on the hogs. For example, the time and labor involved in getting a hog from 30 to 260 pounds is considerably different than going from 60 to 230 pounds. Likewise, feed efficiency (FE) declines as hogs are fed to heavier weights. Growers paid a flat fee plus incentives for FE should restrict in and out weights to a given range or be compensated for deviations from these ranges.

6. Condition and quality of incoming pigs.

- a) The health of pigs when they arrive often determines the mortality and morbidity of the group. The grower responsible for deathloss and/or FE is at a disadvantage if the owner has complete control over the quality of pigs delivered.
- b) If the contract does not allow the grower to refuse pigs at delivery, a different contract or an amendment to the current one may reduce his risk. However, the owner is at great risk if the grower has complete veto power on pigs delivered to the farm. Amendments that may provide a viable compromise include the following:
 - 1) Agree upon a pre-approved feeder pig source.
 - 2) Have the owner stand all deathloss that occurs in the first few days, i.e., one week.

- 3) Have a higher unpenalized deathloss for commingled or stressed pigs. For example, three percent for farm fresh pigs and six percent for others.

7. Health care and deathloss.

- a) The contract should clearly state what health care practices are expected of the producer as well as the procedure to follow should health concerns arise. Problems may result when the grower is penalized for mortality and morbidity but only the owner or his field worker is authorized to call the veterinarian. Likewise, if the producer is not paying the vet bill but is rewarded for performance, he may be tempted to cry wolf too often.
- b) Procedures for reporting and accounting for deathloss should also be included in a contract. Typically, dead animals must be inspected by the owner or field worker. Deaths for which the owner is responsible (in transit, shortly after delivery, during loading) are also important and should be stated.

8. Compensation and incentives.

- a) The amount and timing of payment to the grower should be clearly defined. Some contracts call for two payments, at delivery and at removal, others require monthly payments, and still others have only one payment.
- b) The incentive schedule for feed efficiency and/or deathloss should also be explained. Some contracts have a threshold level of performance, while others have a graduated schedule. Incentives may be either in the form of a bonus for good performance or a penalty for poor performance.
- c) Scale tickets for incoming and outgoing weights and feed usage should be provided to the grower to insure that he is paid for the appropriate FE and deathloss.

9. Ownership, inputs, and expenses.

- a) The contract should clearly state who holds title to the hogs—the owner, the grower, or both.
- b) Define which party chooses the inputs—not only which brand, but also who chooses the amount and timing of an input, i.e., medications.
- c) The responsibility of expenses for each party must also be defined. In addition, the owner may not pay for an input that was not approved ahead of time.
- d) Specify which party is responsible for casualty and liability insurance. Also determine how damages to the grower's facility caused by the owner's hogs will be handled.
- e) Define which party is responsible for environmental risks such as manure spills, improper application, or storage and odor complaints. Typically, the grower owns the manure and can apply it to his crops. The grower is also responsible for the manure.

10. Credit risks.

- a) Because little can be done after the fact to correct a problem, both parties should be allowed to gather financial information about the other. This may be best handled on a document separate from the production contract.
- b) Problems and risks that may arise include the following:
 - 1) Except for the right to remove the hogs, the owner is an unsecured creditor of the feeder. The owner has little chance in recovering losses resulting from excessive deathloss.
 - 2) The feeder has a statutory lien in the hogs, but this lien is subject to all prior liens of record. This means that the owner's secured creditor can remove the hogs without paying the grower. Once the hogs are removed, the grower has an unsecured claim for his contract damages which is probably uncollectible.

- c) Keep in mind that a parent company is typically not responsible for the debts of a subsidiary.
- d) It is possible for the grower to receive first lien on the hogs if the owner and his creditors are willing to give the grower a lien subordination.

Summary

The success or failure of contract production for the farmer depends on the provisions of the contract. The contract should be written clearly and concisely, and offer advantages for both parties. As an individual considers a contract, he/she should determine if it allows him to capitalize on his/her strength, reduces his/her exposure to unfavorable outcomes, and adequately compensate him/her for his/her inputs. Successful contracting arrangements require that the farmer knows his/her cost of production before the contract is signed and pays attention to detail afterward. While a good contract is essential, it is also important that both parties are professional and willing to work out problems that may arise.