Overview of of Uniform Marketing Agreements

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File C5-87

Cooperatives use uniform marketing agreements to ensure that a specified amount of product is marketed to the cooperative. This reduces raw product supply risks, which typically enhances a cooperative's ability to obtain debt financing. Information File C5-88, [Sample Uniform Marketing and Delivery Agreement](www.extension.iastate.edu/agdm/wholefarm/pdf/c5-88.pdf), www.extension.iastate.edu/agdm/wholefarm/pdf/c5-88.pdf, provides an example agreement.

A member's delivery of product is assured because most states have enacted statutes governing uniform marketing agreements that provide that a cooperative is entitled to specific performance and injunctive relief, as well as monetary damages, against a member who fails to meet delivery obligations. Further, some state statutes impose penalties against persons or entities that attempt to purchase the agricultural products committed to the cooperative or divert such products to other markets.

As in any contractual relationship, the uniform marketing agreement creates certain duties and rights between the parties. However, unlike the traditional two-party contract that only creates rights between the contracting parties, uniform marketing agreements create an additional duty to the other members of the cooperative. Also, where a state statute governs a uniform marketing agreement, this statutory authority may provide more extensive remedies for a breach of delivery of an agricultural commodity than would be allowed under traditional contract law or the Uniform Commercial Code.

Given the current importance of uniform marketing agreements, this summary will review and discuss (1) the legal characterizations and duties created by a uniform marketing agreement, (2) what constitutes a breach of a uniform marketing agreement, and (3) the consequences of a breach. This summary does not constitute legal advice. Parties contemplating entering into a uniform marketing agreement should consult with competent legal advisors.

Legal Characterizations and Duties Created

The typical marketing agreement obligates the member to deliver products to the cooperative and obligates the cooperative to market or otherwise utilize that product. Although marketing agreements differ, they have common elements that mirror statutory requirements and/or the absence of such requirements. The duties and rights created by the contract and the governing statute directly affect what constitutes a breach and the available remedies.

Characterization of Title to the Product. Many states have enacted statutes that address whether the cooperative may or may not take title to the members' products and the manner and time at which title passes where passage of title is required by statute or contract. Most states do not require that title to the product pass to the cooperative, but rather allow the parties to contractually create either a seller-purchaser or principal-agent relationship. Therefore, by carefully drafting the marketing agreement, the parties can create the legal characterization that will best suit their goals. Where the parties' characterization is not ambiguous, courts have usually upheld their intended characterization.

Duty of Cooperative Members Under a Uniform Marketing Agreement. Regardless of the legal characterization created by the uniform marketing agreement, members entering into a marketing agreement owe certain duties and obligations to the cooperative for the term specified in the agreement. In fact, almost all states have provisions addressing the duration and/or termination of such marketing agreements.

The statutory duration of uniform marketing agreements are relatively short compared to the potential duration of cooperatives. Most states limit the marketing agreement to either five years or 10 years. Some states permit the marketing agreement to exist for any period of time. It should be noted that while several state cooperative statutes permit the

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marketing agreement to exist more than five years, many cooperatives draft contracts with a shorter term. Typically, a uniform marketing agreement will establish either a five- or a three-year term, in which either party may terminate the agreement at the end of a given fiscal year by providing notice not less than 30 days prior to the end of that year. After notice of termination, the marketing agreement may provide that one or two years remain under the agreement.

Most state statutes also permit a marketing agreement to require that a member deliver his or her agricultural products to or through the cooperative. Marketing contracts generally require the producer to commit to deliver a specified amount of product. These provisions usually provide that if a member is unable to deliver the specified amount of product, the member is required to obtain the product from another source and deliver it to the cooperative.

If the member does not deliver the product as stated, the agreement may provide that the member agrees that the cooperative, at its option, may act as the member's agent for the purpose of obtaining the product in the name of the member and charge the member for all expenses, including, but not limited to, the price of the product, shipping, and all incidental costs incurred to obtain and deliver the product. Although the cooperative's acquisition at the member's cost may appear punitive, the member is credited for making delivery and is entitled to patronage. Costs in excess of the product's value are typically charged to the member and are deductible from member equities.

Duty of a Cooperative Under a Uniform Marketing Agreement. A cooperative owes specific duties to its members under a marketing agreement. A uniform payment for the product is typically provided to the members that is equal to the resale price of the product after deducting all necessary selling, overhead, and other expenses. The cooperative's articles of incorporation and bylaws, however, usually give directors broad discretion in determining how and when the members will be paid.

The type of payment may have characteristics of initial and final payments that in the aggregate reflect the cost of goods sold or delayed payments that are patronage dividends. Marketing agreements may provide that the cooperative's payment to the member be one of two types and in the discretion of the board of directors. One option is to pay the purchase price of the commodity in cash in an amount determined by the board; another option is to pay the member a unit retain evidenced by non-dividend bearing equity credits or a combination of these two options.

Other duties of the cooperative under the uniform marketing agreement, which may or may not be specifically addressed by state statute, include the duty to accept delivery from the members, the duty to grade and classify product, and the duty to timely market the product. Although marketing contracts may not require a cooperative to accept delivery of the product, the duty may be implied from the cooperative's duty to pay the member for the product. Finally, while many marketing agreements do not provide a time frame in which the product should be marketed, a cooperative should generally market the crop within the crop year.

Consequences of Breaching a Uniform Marketing Agreement

When a member breaches his or her marketing agreement, he or she is subject to several remedies available to the cooperative. These remedies include terminating the member's membership in the cooperative, contract damages, liquidated damages, and the equitable remedies of injunction and specific performance.

Membership Termination. Marketing agreements usually provide that a member's membership in the cooperative will be terminated if certain conditions are not met. For example, the cooperative may require that the members' product meet certain product quality standards. In addition, the contract may provide that failure to patronize the cooperative for one year automatically terminates the member's membership rights in the cooperative. This type of remedy is necessary because of the cooperative's need to receive requisite amounts of a specific type and quality of agricultural products to meet consumer and purchaser demands.

Liquidated Damages. Most statutes authorizing uniform marketing agreements specifically allow an enforceable liquidated damages provision. Liquidated damages provisions have generally been upheld by courts. However, those liquidated damages provisions that are found to be a penalty may be invalidated by the courts.

Equitable Remedies of Injunction and Specific Performance. Almost all state statutes allow a cooperative to obtain an injunction or a decree of specific performance against a member for the breach of a marketing agreement. An injunction against the breaching member helps prevent any further breach of the agreement. Allowing the specific enforcement of the terms of the marketing agreement is a potentially strong remedy that can force a member to deliver the agricultural product as specified in the contract. This remedy helps the cooperative meet its delivery requirements to third parties. Both the remedy of injunctive relief and the remedy of specific performance have been upheld against defenses contesting their validity. Moreover, the remedy of specific performance is available even if the contract contains a liquidated damages provision.

Remedies Available to the Cooperative Against Third Parties. In addition to the remedies available to the cooperative against its members for breach of the marketing agreement, cooperatives typically have remedies available against third parties who induce member(s) to breach the marketing agreement. Statutes penalizing inducement of breach have been held valid and constitutional by the United States Supreme Court. Under such statutes, liability is typically imposed on the inducer only if he or she "knowingly" induces or attempts to induce a member to breach the marketing agreement. The difficult issue faced by the courts is whether the third party "knowingly" interfered with the marketing agreement. Therefore, case law in this area is inconsistent.

Summary

The uniform marketing agreement is a tool used by cooperatives to ensure that a specified amount of product is marketed to the cooperative. Not only are marketing agreements authorized by state statute, courts have consistently recognized their validity. By using a marketing agreement, the cooperative and its producer members (1) can be certain of their respective rights and obligations under the agreement, and (2) know up-front the quantity and grade of the commodity to be delivered, which enables the cooperative to better market and more efficiently process the commodity. This efficiency translates into more income for the producer members. By carefully drafting these agreements, cooperatives and their members can enter into these agreements with considerable certainty that their intentions will be recognized and enforced by the courts.

Sample Uniform Marketing and Delivery Agreement, www.extension.iastate.edu/agdm/wholefarm/pdf/c5-88.pdf

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