

Breeding Change — Legislative Remedies for Contract Growers

Part I: Minnesota State Law

by Randi Ilyse Roth

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Much of American agriculture is moving towards an "industrialized" method of farming. In this model, large corporations own vertically integrated food production businesses. These businesses typically own and/or control virtually every aspect of the food production process, beginning with the facility that produces the seeds or the breeder animals, and continuing all the way through the grow-out, slaughter, processing, packaging, and marketing of the finished food product for grocery store shelves.

The farmers who grow the food for these operations generally work under some sort of contract with the companies and are therefore referred to as "contract growers." Although farmers who are contract growers generally think of themselves as independent operators, from the corporations' point of view the growers comprise a sector of the labor force for industrialized agriculture.¹

Contract growers are encountering many difficulties. Growers say that most of the problems are caused by the companies' unfair practices.² Growers nationwide are beginning to organize to try to find solutions to their problems. They are looking at many types of solutions: political, judicial, and legislative.

This is Part One of a series of articles that will examine some potential *legislative* solutions to contract growers' problems in the poultry industry. The series will concentrate on the poultry industry because that industry is generally viewed as the one in which vertical integration is most advanced and in which contract growers' problems are most severe.

¹ Another sector is comprised of processing plant workers. For a description of their difficulties, see B. Goldoftas, "Inside the Slaughterhouse," *Southern Exposure*, Vol. XVII, No. 2 (Summer 1989), p. 27.

² For a description of some of the typical difficulties that contract poultry growers encounter, see "Contract Farming Breeds Big Problems for Growers," *Farmers Legal Action Report*, Vol. 7, No. 1 (Winter 1992).

This part of the series will explain provisions of some Minnesota state laws that were designed to protect contract growers.³ The series addresses Minnesota laws because growers from many states are looking at Minnesota law as a starting point for drafting a model law for all states. This article will explain that Minnesota law contains some good ideas and some strong provisions—but in many ways it is flawed. Growers who are developing model state laws should analyze Minnesota law very carefully.

Minnesota State Law

Poultry growers view Minnesota's state contract farming law⁴ as being the best law in any state at this time. The Minnesota law certainly does not address all of the growers' concerns, but it is a beginning. This article will analyze the five key provisions of the law: recapture of capital investment, alternative dispute resolution, parent company liability, implied promise of good faith, and licensure. For each of the five provisions, the article will explain the idea behind the law, the precise statutory provisions, the rules that interpret the statute, and the net effect of the provision from the growers' perspective.

Recapture of Capital Investment

The Idea

Poultry companies often ask growers to make substantial capital investments on their farms at their own expense. For example, the company could ask the grower to build an additional chicken house, to install fans, or to change over to a different watering system.

This is very risky for the grower. It is risky for some growers because they have, for example, a seven-year contract. They know that they need at least the entire seven years of profit from the chicken business to pay off the debt on their capital investments. If the company were to choose to terminate their contract for any reason before the seven years were up, the grower would be left with a large debt on a facility that could not be used for any other profit-making business.⁵

Capital investments are even riskier for growers whose contracts last only seven or eight weeks (one flock).⁶ Although the companies typically make *oral* representations that they intend to renew these short contracts "if all goes well," growers are afraid that they will

³ According to current plans, later installments in the series will focus on ideas for a model state law and on reforms that are needed in the federal Packers and Stockyards Act.

⁴ The bill that created the main "Agricultural Contract" law was called the Producer Protection Act. Minn. Stat. § 17.90, *et seq.* The other law discussed in this article is the Wholesale Produce Dealers' Act (WPDA). Minn. Stat. § 27.01, *et seq.*

⁵ People often refer to poultry houses as "single-use" buildings. Growers who have lost their contracts have found it virtually impossible to find a profitable alternative use for the buildings.

⁶ These contracts are common in the southeastern United States.

spend tens of thousands of dollars and then have their growing arrangements ended before the investment bears any fruit. This has happened to many growers.

The "recapture of capital investment" provision of the Minnesota law is designed to offer some protection to growers who are in these situations.⁷

The Statute

There are two parts to the statute.⁸ The first part provides that a company must not terminate or cancel a contract that requires a grower⁹ to make a capital investment in a building or equipment that costs \$100,000 or more and has a useful life of at least five years until certain conditions are met.¹⁰ The conditions are:

- 1) The company must have given the grower *written* notice of its intent to terminate or cancel at least 180 days before the effective date of the termination or cancellation; and
- 2) The grower must have been reimbursed for the damages that he or she incurred by making such an investment.¹¹

The second part of the statute addresses situations in which the company complains that termination is necessary because the grower has breached the contract. The statute provides that if the contract required a capital investment,¹² the company cannot terminate or cancel a grower who has breached the contract until:

- 1) The company has given the grower a *written* notice that lists all of the reasons for the termination or cancellation at least 90 days before the termination or cancellation; and
- 2) The grower fails to correct the reasons stated in the notice within 60 days of receipt of the notice.¹³

There are exceptions to these grower protections in certain extreme situations.¹⁴

⁷ Some who were involved with the promulgation of the law explain that the law was designed to offer protection to growers who are cut off *while a contract is in effect* but that it was *not* designed to help growers who are cut off at the expiration of a contract. This author has not had the opportunity to review the legislative history of the act to confirm that interpretation.

⁸ Minn. Stat. § 17.92.

⁹ The statute applies to "producers" of "agricultural commodities." Both terms are defined in the statute. Minn. Stat. § 17.90, subd. 2 and subd. 4.

¹⁰ Minn. Stat. § 17.92, subd. 1.

¹¹ The investment must have been made for the purpose of meeting the minimum requirements of the contract. Minn. Stat. § 17.92, subd. 1(2).

¹² The term "capital investment" is an investment as described above: an investment of at least \$100,000 in buildings or equipment with a useful life of at least five years. Minn. Stat. § 17.92, subd. 2.

¹³ Minn. Stat. § 17.92, subd. 2.

The Rules

The rules¹⁵ interpret the statute in a manner that weakens grower protections in three significant ways.

First, the statute applies only to situations in which the company *requires* the grower to make a capital investment. The rules clarify the meaning of the word “requires” by providing that the grower must have a “*written* contractual obligation” to make the improvement.¹⁶ This means that when companies use *oral* statements to communicate to growers that they are required to make improvements, the growers are not protected by the law. Growers report that when companies impose such requirements, the company usually communicates the requirement orally, not in writing. Therefore, this rule makes the law inapplicable in most cases.

Second, the statute applies to “termination” and “cancellation” of a contract. Before the rules were promulgated, many interested parties thought that the terms “termination” and “cancellation” were meant to apply to two different situations. It was assumed that one term applied to situations in which a company ends a growing arrangement while a contract is still in effect, and that the other term applied to situations in which a company decides *not to renew* a short contract that expired (for example, a contract that covers only one flock). The rules did not interpret the statute in that way. The rules provide that “ ‘[t]ermination’ and ‘cancellation’ do not include *expiration* of the contract.”¹⁷ Therefore, when a company decides not to place another flock after the expiration of a one-flock contract, this law offers no protection; the law only offers protection to growers who are cut off while a contract is in effect. A company that uses one-flock contracts can entirely circumvent this law by waiting until the end of a flock—which is never more than a few weeks—to cut off the grower.

Third, the statute did not explain how “damages” are to be computed. The rules explain that damages “do not include payment for the reasonable useful life of an asset that extends beyond the term of the contract.”¹⁸ This seems to mean that the grower can recover the profit that he or she could have expected to make from the investment during the duration of the contract. It is unclear whether this rule would be interpreted to imply that a grower cannot recover out-of-pocket expenses as part of his or her damages.

¹⁴ The requirements for the 180-day and 90-day notice periods described above are waived and the contract may be terminated or cancelled immediately if the alleged grounds for termination or cancellation are either (1) voluntary abandonment of the contract relationship by the grower; or (2) conviction of the grower for an offense directly related to the business conducted under the contract. Minn. Stat. § 17.92, subd. 3.

¹⁵ Minn. Rules, § 1572.0030.

¹⁶ Minn. Rules § 1572.0030, subpart 1 (emphasis added).

¹⁷ Minn. Rules, § 1572.0030, subpart 1 (emphasis added).

¹⁸ Minn. Rules, § 1572.0030, subpart 1.

The Net Effect

The "recapture of capital investment" law is a good idea, but, as a practical matter, it is not much help to growers in its current form. The statute is very restrictive because it applies only to investments of \$100,000 or more.¹⁹ And, as described above, the additional restrictions in the rules make it extremely unlikely that this law will be of benefit to growers.

Alternative Dispute Resolution

The Idea

When poultry growers have disputes with their companies, they often feel that they have no where to turn. In general, they cannot afford to hire lawyers, and they have great difficulty finding lawyers to represent them on a contingency fee basis. Poultry growers need an affordable way to resolve disputes fairly.

The Statute

The statute²⁰ addresses this problem by providing that every contract "must contain language providing for resolution of contract disputes by either mediation or arbitration."²¹

The Rules

The rules²² simply lay out the details of how the mediation or arbitration arrangements shall be made.²³ The rules provide that this alternative dispute resolution law applies only to contracts signed after August 1, 1990.

The Net Effect

It is difficult to gauge the effect of this law. Depending upon the specifics of the case, an alternative dispute resolution clause could be a benefit or a detriment to the grower. For example, a grower who has an opportunity to litigate before a sympathetic judge will not want to resolve the dispute in an arbitration forum. On the other hand, mediation and even arbitration are generally less expensive procedures than litigation; a grower who cannot afford to hire an attorney to file a lawsuit may be able to afford to hire an attorney to represent him or her in a mediation.

¹⁹ Many of the capital investments that growers are required to make cost \$20,000 or \$30,000.

²⁰ Minn. Stat. § 17.91.

²¹ Minn. Stat. § 17.91. Because poultry companies must be licensed in Minnesota, Minn. Stat. § 27.03, and all contracts between companies ("wholesale produce dealers") and growers must be filed with the State Department of Agriculture, Minn. Stat. § 27.04, subd. 2(b) and Minn. Rules § 1572.0020, subp. 7, the state has a mechanism for enforcing this provision.

²² Minn. Rules, § 1572.0020 and § 1572.0010, subpts. 2 and 5.

²³ There are exceptionally detailed rules for arbitrations regarding seed contracts.

Under this law, contracts may provide for either mediation, which is not binding, or arbitration, which is binding.²⁴

Parent Company Liability

The Idea

Sometimes the company that contracts with a grower is a small company that is a subsidiary of a larger company. The Minnesota State Task Force that studied problems with contract farming concluded that in some cases the smaller companies failed to pay the growers and became bankrupt, leaving the growers with no recourse.²⁵ This statute is designed to make it possible for growers in this situation to recover from the parent company.

The Statute

The statute simply says that if the contracting company is:

[T]he subsidiary of another corporation, partnership, or association, the parent corporation, partnership, or association is liable to a seller for the amount of any unpaid claim or contract performance claim if the contractor fails to perform according to the terms of the contract.²⁶

The statute does not define "subsidiary" or "parent company."

The Rules

The rules²⁷ define parent company as an entity²⁸ that owns²⁹ more than 50 percent of the common or preferred stock entitled to vote for directors of a subsidiary corporation or provides more than 50 percent of the management or control of a subsidiary.³⁰

²⁴ As a practical matter, this means that the company chooses whether the forum is mediation or arbitration, because in most cases the company drafts the contract and offers it to growers on a "take it or leave it" basis.

²⁵ Agricultural Contracts Task Force, Final Report to the 1990 Legislature (Feb. 1990), Minnesota Department of Agriculture (90 West Plato Boulevard, St. Paul, Minnesota, 55107), pp. 1 and 3.

²⁶ Minn. Stat. § 17.93. The statute also provides that if the company is required to be licensed to purchase agricultural commodities, the licensing authority may require the parent company to guarantee payment or contract performance as a condition of licensing.

²⁷ Minn. Rules, § 1572.0040.

²⁸ The entity must be a corporation, partnership, sole proprietorship, or association. Minn. Rules § 1572.0040.

²⁹ This "ownership" can be through ownership of capital stock, cumulative voting rights, voting trust agreements, or any other plan, agreement, or device. Minn. Rules § 1572.0040.

³⁰ Minn. Rules, § 1572.0040, emphasis added.

The Net Effect

It seems that this law would effectively address the problems that it was designed to address.

Implied Promise of Good Faith

The Idea

Growers report that there are many ways in which the company can take actions that benefit the company at the growers' expense. In some instances the actions are acceptable within the business relationship, but in other instances the actions constitute bad faith. Before the passage of this law, if companies took action in bad faith that caused harm to the grower, but the companies' actions were technically within the letter of the law, the grower had no recourse.

The Statute

The statute³¹ provides that there is an implied promise of good faith by all parties in all agricultural contracts. It states that in an action to recover damages for a breach of this promise of good faith, damages, court costs, and attorney fees may be recovered. The definition of "good faith" is "honesty in fact in the conduct or transaction concerned."³²

The Rules

There are no rules interpreting this part of the statute.

The Net Effect

This is a very powerful law that could provide significant assistance for growers. For example, growers who relied on oral promises that the company made and then broke could proceed under this law. The attorney fees provision makes this law especially useful because it should make lawyers more interested in taking growers' cases on a contingency fee basis.

Licensure

The Idea

The idea behind licensure is that if a company must be licensed, the state has an easy, quick method for enforcing the laws with which the company is required to comply.

The Statute

In Minnesota, poultry is defined as "produce."³³ The Wholesale Produce Dealers Act requires that all produce dealers—and therefore all poultry companies—must be licensed.³⁴

³¹ Minn. Stat. § 17.94.

³² The statute provides at Minn. Stat. § 17.94 that "good faith" is defined at Minn. Stat. § 336.1-201, subsection (19).

³³ Minn. Stat. § 27.01, subd. 2(3).

It is significant that the companies must be licensed because companies are in danger of losing their licenses if they commit any one of several violations.³⁵ The violations concern a wide range of issues, including the making of false statements,³⁶ the violation of the terms of a contract,³⁷ and the failure to make payment in full according to commitments.³⁸

The Rules

The rules make this law an even stronger protection for growers.³⁹ The rules contain a list of "unfair trade practices"; if a company commits any of the unfair practices on the list, the company is in danger of losing its license. The list includes such items as:

- Making a false or misleading statement for a fraudulent purpose, including statements made to induce a person to sign a contract;⁴⁰ and
- Using coercion, intimidation, the threat of retaliation, or the threat of contract termination to impose, demand, compel, or dictate the terms, payment or manner of payment, or the signing of a contract by a producer.⁴¹

The Net Effect

The net effect is that this licensure provision is potentially a very strong law for protecting growers. Of course, the strength of the law depends upon the enforcement actions taken by the Department of Agriculture; but with a conscientious enforcement staff, this law should be of great value to growers who have been treated unfairly.

³⁴ There is some question as to whether this statute applies to the typical poultry growing situation in which the grower does not *own* the birds, and therefore cannot technically "buy" or "sell" them. The problem arises because the statutory definition of "wholesale produce dealer" focuses on entities that "buy or contract to buy." The legislature attempted to clear up this problem with a recent amendment that was designed to make the statute applicable to grow-out arrangements in which the grower does not own the poultry. The amendment did not define the word "buy," but it did define the word "seller" as "a farmer or wholesale produce dealer, whether the person is the owner of the produce or produces it for another person who holds title to it." Minn. Stat. § 27.01, Subd. 10.

³⁵ Minn. Stat. § 27.19.

³⁶ Minn. Stat. § 27.19, subd. 1(a)(2).

³⁷ Minn. Stat. § 27.19, subd. 1(a)(5).

³⁸ Minn. Stat. § 27.19, subd. 1(a)(12).

³⁹ Minn. Stat. § 27.14 gives the commissioner the power to make rules for carrying out and enforcing certain provisions of the Wholesale Produce Dealers' Act (WPDA) and for governing the rates charged by, and the buying, selling, advertising and trading practices of wholesale dealers. Pursuant to that authority, the Department has promulgated rules that constitute "unfair trade practices" under the WPDA.

⁴⁰ Minn. Rules, § 1500.1401(A).

⁴¹ Minn. Rules, § 1500.1401(D).

Conclusion

Growers in Minnesota have more state law protection than growers in any other state that we know of. The Minnesota law is a good starting place for gathering ideas for a model contract farming law, but it should not simply be copied. A later article in this series will put forth suggestions for additional provisions that should be considered in the drafting of a model law.