

Agribusiness Alert: The Long Awaited Final GIPSA Rules Published Regulating Poultry and Livestock Production Contracts

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On Friday, December 9, 2011, the United States Department of Agriculture published final rules that will implement certain directives of the 2008 Farm Bill. The 2008 Farm Bill ordered the Secretary of Agriculture to establish criteria for determining if conduct by a live poultry dealer, a packer or swine contractor violated the Packers and Stockyard Act (the PSA). Notably, the final rule issued last week was modified substantially from the rule proposed by the USDA's Grain Inspection Packers and Stockyards Administration (GIPSA) back on June 22, 2010. Sweeping changes were made after the USDA reviewed more than 61,000 comments filed and as the result of strong opposition from the meat and poultry industries and Congress to the proposed rules.

The final rule establishes criteria for GIPSA to consider when determining if a violation of the PSA occurred under the four separate categories described below. The final rule also clarifies that when applicable to live poultry dealers, the rules apply to all stages of a live poultry dealer's poultry production, including pullets, laying hens, breeders, and broilers, excluding egg-type pullets, hens that only produce table eggs, and breeder flocks for the egg industry. **The final rule will apply to all poultry growing arrangements, swine production contracts, or any other regulated livestock or poultry contracts entered into, amended, altered, modified, renewed or extended after February 7, 2012.** The final rules are effective on February 7, 2012.

Suspension of the Delivery of Birds: Notice Requirement

The final rules imply that a live poultry dealer must give reasonable notice to a grower prior to the suspension of any bird deliveries. The final rule establishes criteria for determining whether a live poultry dealer has provided reasonable notice.

Among the criteria which may be considered includes: (a) whether a live poultry dealer provides a poultry grower written notice at least 90 days prior to the date it intends to suspend delivery of birds under a poultry growing arrangement; (b) whether the written notice adequately states the reason for the suspension of delivery, the length of the suspension of delivery, and the anticipated date the delivery of birds will resume;



and (c) whether a catastrophic or natural disaster, or other emergency, such as an unforeseen bankruptcy, has occurred that has prevented a live poultry dealer from providing reasonable notice.

For live poultry dealers that are considering suspending the delivery of birds to a grower, the dealer should provide written notice to the growers that comply with these new rules.

Additional Capital Investments

The final rules also regulate when poultry and swine contractors may require contract growers to make capital improvements or "additional capital investments" to their swine or poultry operations, and if those additional requirements are a violation of the PSA. The final rules establish criteria for determining whether a requirement of additional capital investment over the life of a poultry growing arrangement or swine production contract violates the PSA. The rules define "additional capital investment" to mean any requirement of \$12,500 or more per structure, but the definition excludes the costs of maintenance or repairs.

Among the criteria which may be considered are whether: (a) the grower is given the option to make the investment; (b) the investment is in retaliation or coercion; (c) the packer or swine contractor substantially reduces or terminates operations within 12 months of requiring a grower to make such improvements absent a natural disaster, emergency, or unforeseen bankruptcy; and (d) the costs of the required investment can be reasonably expected to be recovered by the grower.

It is not clear from the final rules when such additional capital investments are "required," thus triggering application of the rules. For example, under Minnesota law, a capital improvement is "required" only if there is an express contractual obligation to make the improvement. Live poultry dealers and swine contractors should consider requiring growers to execute an addendum to the growing contract if, and when, an additional capital contribution will be required of the grower. This addendum should expressly acknowledge: (a) that the grower had the discretion not to make the additional capital investment; (b) the grower's agreement to contribute the additional capital investment was not the product of coercion, retaliation, or threats of coercion or retaliation made by the live poultry dealer or swine contractor; and (c) the grower performed an independent financial review of the additional capital requirement as to whether the additional capital investment can be reasonably expected to be recouped and the grower reasonably expects the investment to be recovered.

Reasonable Period for a Grower to Remedy a Breach of Contract

The final rules also imply that a swine contractor and live poultry dealer must give the grower a reasonable opportunity to cure or remedy any breach of the production contract, with a few exceptions. The final rule establishes criteria to determine whether a swine contractor or live poultry dealer



has provided a reasonable period for a grower to remedy a breach of contract that could lead to termination of a production contract.

In determining if a live poultry dealer or swine contractor has provided a reasonable period of time for a grower to remedy a breach of the contract, the Secretary may consider if: (a) the contractor has provided a written notice of the breach of the contract providing the grower with a description of the breach; (b) the remedial action required to cure the breach; and (c) the time period within which such action must be taken. In addition, the Secretary may consider whether the termination notice provided the grower adequate time to rebut the allegation of a breach.

Live poultry dealers and swine contractors should review and revise their grower contracts to ensure the contracts address the criteria set forth in the rules. Live poultry dealers and swine contractors should also consider revising production contracts to include a provision in which the grower acknowledges that the cure period provided in the contract is in fact reasonable. Although the final rule does not limit the ability of a live poultry dealer or swine contractor to terminate a production contract where food safety or animal welfare issues are raised, there is no exception for environmental emergencies. Thus, production contracts may need to be revised to include a provision that expressly allows for the termination of the contract and allows access to the grower's facility in the case of an environmental emergency.

Arbitration

Finally, the final rules regulate arbitration clauses in production contracts, and whether those arbitration clauses are a violation of the PSA. The final rules set forth that contracts requiring arbitration include language on the signature page of the contract that allows a producer or grower the right to decline arbitration. The final rule also establishes criteria for GIPSA to consider when determining if the arbitration process provides a meaningful opportunity for growers and producers to participate fully in the arbitration process.

Under the rules, the production contract must disclose in bold and conspicuous print the costs of arbitration to be borne by the grower, together with any limitations on the grower's legal rights so as to permit the grower to make an informed decision on whether to agree to arbitration. The contract must also provide the grower with an opportunity to opt out of arbitration. If the grower does not affirmatively accept the arbitration provisions set forth in the contract, he will be deemed to have opted out of arbitration. Finally, the rules provide an opportunity for the USDA to assess the allocation of costs, whether the grower may obtain access to information from the packer or swine contractor, and whether a written opinion based upon the applicable law is required.



Live poultry dealers and swine contractors should review and revise their production contracts to comply with the final rules. It is important to note that the final rules do not establish safe harbors for live poultry dealers and swine contractors with regard to arbitration provisions contained in their contracts. In fact, in its explanation of the arbitration provisions, the USDA describes the rule as "establishing a list of some of the criteria the Secretary may consider" in determining if a contract's arbitration provisions violate the PSA. Thus, poultry dealers and swine contractors should be careful in imposing any costs, barriers, impediments, or limitations on the use of arbitration by growers in their production contracts.

Respective state laws should also be considered. For example, under Minnesota law, production contracts must contain a provision that allows the grower to choose either arbitration or mediation. Under the final GIPSA rules, if there is an arbitration clause in the contract, the grower may elect not to proceed with arbitration. Therefore, in Minnesota, the grower must be offered the choice between arbitration, mediation, or to just proceed with a civil lawsuit. Since Minnesota law requires that arbitration must be offered in the contract, to comply with the final GIPSA rules, the contract must also provide the arbitration process and some estimate as to the costs of arbitration. Minnesota has a specific arbitration procedure, so the contractor may want the contract to default to this statute (rather than defining a separate arbitration process in the contract). Because of overlapping state and federal laws, the final rules that relate to arbitration become involved.

Gray Plant Mooty is a full-service law firm representing agricultural clients in compliance and contracting issues under state and federal laws, including compliance and contracting issues under the Federal Packers and Stockyard Act. Contact Philip Kunkel or Jeffrey Peterson if you have any questions related to the Packers and Stockyard Act and the final GIPSA rules.

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