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Duration, Termination & Cure

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CHAPTER QUICK TIPS

Beware of Termination Clauses

Watch out for provisions that allow termination for any reason or for minor contract violations. These provisions can be replaced with language allowing termination only in cases of serious breach by the farmer or buyer. This kind of breach is often called “material breach.”

“Discretion” Is Code for “Whatever I Want”

The term “discretion” is often used in contracts. “Discretion” usually means that one party has the power to make whatever choice it wants to make about a particular topic. Farmers should be careful if a contract gives the buyer “discretion” in any respect.

DURATION: HOW LONG WILL THE CONTRACT LAST?

When does the contract begin and end?

Be sure to understand when the contract begins, or “becomes effective.” All of your contract obligations begin on the day the contract begins, so it is important to know when you have to start making sure you are complying with the contract terms.

Make sure you understand exactly how long the contract is intended to last. Some contracts state clear start and end dates. Others are seasonal, and still others are renewable every year or every few years. Some contracts are more vague, using production cycles to determine length of the contract. For example, the duration of egg and poultry contracts is typically measured in numbers of flocks. If you have a flock-to-flock contract, especially for broilers, these contracts can be terminated after a very short period of time.¹

Can the contract be renewed?

Does the contract have a renewal provision? If so, how is the contract renewed? Is it automatic, or does it require some sort of action by one or both parties? If you understand how renewal of the contract could happen, you will be less likely to become locked in an unfavorable contract by unintentionally triggering renewal, or miss an opportunity to maintain a positive contract relationship by unintentionally failing to renew.

If the contract does not have a renewal provision, consider whether you might like to add one that could make it easier to maintain an important contract relationship. Be sure to clearly state the conditions for renewal and how renewal could be accomplished.

Will the contract last long enough to allow you to recover any investments?

Before signing, consider carefully whether the contract period is long enough for you to recover any investments you must make to carry out your contract obligations. If the commodity you will be producing and selling under the contract requires you to make investments—purchasing specialized equipment, constructing new facilities, etc.—you should carefully consider the contract duration and whether the buyer will have the power to terminate the contract early (see next section). If the contract could end before you have the chance to recover your investment from earnings under the contract, how will you replace that income? Can you rely on there being another market or buyer for your production after the contract ends? If not, you may wish to reconsider the risk you are taking by entering into a contract that requires investment but can end before you recover your costs.

TERMINATION: COULD THE CONTRACT END EARLY?

Most contracts include at least a few ways a contract could terminate before its natural endpoint. Termination provisions are often complicated and might be scattered throughout the contract documents. It is important to fully understand how and when your contract could be prematurely terminated so you do not unintentionally lose a contract you are depending upon.

It is smart to go through the contract and identify all of the ways the contract could end earlier than expected.

Types of termination clauses

Termination at Will

Sometimes, a contract states that it can be terminated at any time and for any reason. Usually, but not always, the party who wishes to terminate the contract for any reason is required to provide advance written notice of termination to the other party.

- *Termination for Any Reason, Without Notice*

You should think carefully before entering into a contract that can be terminated for any reason, at any time, without notice. This type of contract can evaporate without warning. Thus, if your goal is to obtain financial security for the upcoming months, this kind of contract will not help you. However, if you are not worried about the deal falling through (perhaps because you have other marketing options or because you believe the buyer truly needs your production), a contract like this can at least lay out the ground rules if the contract ends up being fully performed.

Regardless, you should be aware that signing a contract that can be terminated at any time without notice could leave you without a buyer in a heartbeat. It would be better to at least negotiate a notice period, as discussed below.

- *Termination for Any Reason, With Written Notice*

Although it is risky to sign any contract that can be terminated for any reason, requiring a written notice period at least gives you some time to look for a new buyer.

Example: Termination for Any Reason With Written Notice

The Buyer may terminate this Agreement, with or without cause, at any time, upon 90 days' prior written notice to the other.

Note that this language gives only the buyer the power of termination—the farmer has no termination power. This language would be more favorable if you replace “The Buyer...” with the phrase “Either party...”



If the contract allows for termination for any reason after a written notice period, make sure the notice period is long enough for you to find another buyer or take whatever other steps you need to continue your operations without too much disturbance. For example, 30 days' notice might be too short, while 90 days' notice might be adequate.

Blanket Breach: Termination for Any Contract Violation

Instead of allowing parties to terminate a contract at will, contracts often limit termination to situations where one party has violated—or “breached”—a contract provision. The broadest of these provisions allow termination for any breach (major or minor) of any contract provision. These so-called “blanket breach” provisions are risky because even a trivial contract violation that does not affect the main purpose of a contract (buying and selling organic crops or livestock) could lead to termination.

In a blanket breach situation, non-breaching parties are not required to terminate due to a breach, but they have the power to do so. For example, if the contract specifies that notification must be sent by certified mail but one party uses registered mail, the other (non-breaching) party could use this minor breach to get out of the contract if the contract also contains a blanket breach termination clause.

Be aware that signing a contract with this type of provision can make any less-than-perfect contract performance a potential problem.



Example: Blanket Breach Termination

Default, Breach: Each party may terminate this Agreement if the other party breaches any part of this Contract.

Farmers who encounter this type of provision should seriously consider trying to negotiate deletion of the provision or change to require “material breach” (discussed on page 5–7 of this chapter) as a termination trigger.

- *The Risk of Blanket Breach Termination Provisions in Combination With Vague Contract Provisions*

As discussed in Chapter 3 of this guide, contract language that is vague or unclear can create significant problems when differences arise. This is particularly true if the contract states that it can be terminated if any part of the contract is breached. You may believe that you are fulfilling all of the contract requirements, but if the buyer understands the requirements differently because the language is unclear, the buyer could claim that there is a breach and seek to terminate the contract. The danger from the combination of vague requirements and blanket breach termination can be difficult to spot when first reviewing a contract because often the termination clause is in one section of the contract and the vague provision is in another section.

Example: Blanket Breach + Vague Provision

One part of the contract states:

D (4). Producer agrees that farm premises shall be kept in an aesthetically pleasing condition.

And, in another section, the contract also states:

J (1). Buyer may terminate this agreement if Producer breaches any term described herein.



A contract with the provisions in the example above could easily allow a buyer to terminate by claiming that your farm is not “aesthetically pleasing” on a particular day. This claim is hard to defend against because “aesthetically pleasing” is a vague term that means different things to different people.

A more subtle way that this combination of provisions could cause difficulty is if a buyer attempts to use a minor breach as leverage. For example, a buyer could say, “Well, you committed a minor contract breach, and I could cancel the contract...but I won’t if you agree to accept a lower price.” In that situation, unless the buyer is bluffing, you are faced with the unpleasant choice between no contract and a lower price.

**If You Encounter a Blanket Breach Termination Provision:**

- Replace it with a provision that allows termination only for material breach—not for minor breaches. See below for a discussion of material breach.

If you cannot replace the term with a material breach term:

- Try to get the blanket breach term deleted.

If You Encounter a Blanket Breach Termination Provision + Vague Provisions:

- In addition to the recommendations above on blanket breach, try to make the vague provisions more specific. For example, instead of agreeing that your farm will be kept in an “aesthetically pleasing condition,” you could agree that, “Trash will be removed from farm buildings daily.”

Or, if you cannot clarify vague provisions:

- Try to delete the vague provisions.

Termination for Material Breach

Because contract termination can cause serious financial loss, some farmers may never feel comfortable signing a contract that can be cancelled for any reason, even with a long notice period. Similarly, the risk of termination for even a trivial violation may make a blanket breach termination provision unappealing. As an alternative, consider negotiating a provision that allows the contract to be terminated only if certain, significant contract requirements are not met (“material breach”).

So-called “material breach” is a contract violation that has a significant effect on contract performance and damages or destroys the value of the contract for the other party. Material breach generally involves the timing, quantity, and quality of delivering what was promised and is not concerned with how the parties carry out their obligations. However, parties can also specifically identify as “material” any requirements that might not seem significant but that

they particularly want to be carried out to the letter. For example, a buyer might specify that the farmer's failure to use a particular mix of feed would be material breach, or that a farmer's failure to provide notice of potential crop loss within a certain period would be a material breach.

Example: Termination Only Upon Serious (Material) Breach

Either party may terminate the contract only upon the other party's material breach of the agreement.



Some contracts provide for termination based either on any (blanket) breach or only for material breach depending on the timing or other measurable factors. For a non-agricultural contract, the type of termination available might depend on how long the contract has been in effect or how much of the contract has been fulfilled. For agricultural contracts, the line between termination for any breach and termination only for material breach is typically determined by the production cycle for the commodity under contract.

Example: Termination for Any Breach or Material Breach Depending on Time in Production Cycle

Either party may terminate the contract upon 60 days' written notice for any reason prior to the Grower commencing planting. After Grower commences planting, the contract may be terminated only upon the other party's material breach.



Does the farmer have termination power?

Termination provisions might allow either party to terminate the contract under certain conditions. However, some contracts are one-sided and allow only the buyer to terminate the relationship.



Example: Buyer-Only Termination Provision

The Buyer may, in its sole discretion, terminate the instant Agreement at any time.



“Discretion” Is Code for “Whatever I Want”

The term “discretion” is often used in contracts. In a contract, “discretion” usually means that one party has the power to make whatever choice it wants to make about a particular topic. In the example above, “in its sole discretion,” means the buyer can terminate the contract at any time, for any reason.

Farmers should be careful if a contract offer gives the buyer “discretion” in any respect.

Review the contract termination provisions carefully to determine whether the contract allows you to protect yourself if problems arise or the buyer fails to keep important contract promises. If not, consider negotiating language to protect yourself.

Termination for Buyer’s Failure to Keep Contract Promises

Suppose you are contractually obligated to plant a certain type of identity-preserved seed, and the buyer fails to deliver the seed on time. As a result, you face missing an important planting window and ending up without a crop (or with a low-quality or low-yield crop). In that situation, it would be helpful if the contract gave you an avenue to exit the contract relationship in time to plant substitute seed.

As discussed in Chapter 3, however, termination is not the only possible response to a buyer’s failure to keep contract promises. Because you may ultimately want to continue with the contract even after the buyer’s breach, consider including language that allows you to choose a less severe penalty, such as money damages or a relaxing of your own obligations.

Termination Upon Buyer's Purchase or Merger

If the identity of the buyer you are dealing with matters to you, consider negotiating a provision that would allow you to terminate the agreement if the buyer is bought by or merged into another company. Consider whether it is important for you to have termination power in this kind of situation.

Termination Upon Buyer Becoming Insolvent or Filing for Bankruptcy

Organic contracts frequently state that they may be terminated if one party becomes insolvent, enters bankruptcy proceedings, or otherwise goes out of business.

Example: Termination Upon Insolvency or Bankruptcy

Upon written notice, either party may terminate this Agreement if the other party becomes insolvent, makes a general assignment for the benefit of creditors, becomes subject to any bankruptcy proceedings, has liquidated, or has ceased operations.



However, if a party to a contract files for relief in bankruptcy, bankruptcy law may override the type of termination clause shown in the box above. In most cases, bankruptcy law will allow the buyer in bankruptcy (known as the “debtor in possession”) or the bankruptcy trustee to assume or reject the contract as they wish.² If the buyer in bankruptcy or the trustee assumes the contract, the contract would continue despite the bankruptcy termination clause. If they reject the contract, the contract would be terminated even if the farmer wanted to continue the contract relationship. Because bankruptcy is a complicated and technical area of law, if the buyer files bankruptcy, it would be a good idea for you to consult a bankruptcy attorney.³

See Chapter 12 for more detailed information about both farmer and buyer bankruptcy issues, including some ways to get paid while the buyer is in bankruptcy. The bottom line is that bankruptcy is very complicated, making it all the more important for farmers to investigate the financial stability of the buyer before signing a contract.

Termination Upon Farmer's Serious Illness or Death

If you become seriously ill or disabled, can you terminate the contract, with or without penalty? If you pass away during the contract term, will the contract end? If one of these terrible things comes to pass, would your farm business or your family be forced to shoulder the remaining contract obligations, or might they want to continue under the contract but be denied the opportunity? Consider whether you should try to negotiate a provision protecting you and your family if you are no longer able or alive.



Example: Termination Upon Serious Illness or Death

Upon Grower's serious illness, disability, or death, Grower (or Grower's estate) shall have the power to terminate the contract upon written notice.

This provision allows your family or the person representing your estate to terminate the contract if they so choose, but does not require termination.

Do you have any rights or responsibilities after termination?

Rights:

If the contract is terminated early, will you be reimbursed for your efforts up to the date of termination? The answer is: "Maybe, but probably only if you have provided the buyer with something of value as part of the contract relationship."

Most organic contracts do not expressly provide for reimbursement for farmer efforts upon early termination. Contracts that do provide for reimbursement upon termination almost always involve the farmer providing some sort of valuable service or product to the buyer before the end of the contract period. For example, if you provided consulting services or delivered organic crops or livestock before the contract's early termination, the contract might require the buyer to pay you for the value of those services or products even if the contract terminates early.

However, even if the contract does not expressly require payment for services or goods provided to the buyer in an early termination situation, courts generally require parties who have benefited under a contract to

compensate the other party for those benefits, even if the contract is terminated or made unenforceable. This is called “preventing unjust enrichment.” Still, it is important to note that, if the buyer will not voluntarily pay you for those services or products, you will likely have to go to court in order to get paid.

Note that courts will generally not require a buyer to pay for work done by a farmer prior to early termination that does not benefit the buyer. For example, even if you expend thousands of dollars and hundreds of hours planting, tending, and harvesting an organic red wheat crop, if the contract terminates before you deliver the crop, the buyer will likely owe you nothing under an unjust enrichment theory because you have not yet provided the buyer anything of value (the wheat).

Responsibilities:

If you could be left with expensive or time-consuming responsibilities should the contract be terminated, consider whether your operation could survive that kind of disruption or financial burden. For instance, would you be required to reimburse the buyer for seed or other inputs if the contract is terminated early?

Alternatively, are you required to send seed, plants, breeding stock, or other inputs to back to the buyer if the contract is terminated? Some buyers include this type of provision to protect their interest in identity-preserved seed or breeding stock. Unfortunately, this type of requirement could cause serious disruption to your operation if you are not allowed to bring your crops to harvest or your livestock to full growth. In this situation, consider negotiating different language—perhaps a provision that allows you to choose between reimbursing the buyer for the cost of inputs and sending back seed, plants, or other inputs.

Organic contracts may also specifically state that certain provisions are intended to continue in effect after termination. For instance, a confidentiality clause that states it extends three years past the end of the contract would still be in force even after an early termination. Sometimes a contract includes a list of the provisions in the contract that are intended to continue in effect even after termination.



Example: Provisions Surviving Termination

Survival of Termination. The following sections shall survive termination of this Agreement: A, F, G(ii), J, and L(i)(a).

When deciding whether to enter into an organic contract, be sure to consider whether any responsibilities that survive the contract will interfere with your future operation.

CURE: CAN YOU FIX A BROKEN CONTRACT PROMISE?

Sometimes, a contract will set out how a broken contract promise can be fixed. Fixing a broken contract promise is called “cure,” or “curing a breach.” A cure provision creates a middle ground for the non-breaching party between accepting the breach and having to terminate an otherwise desirable contract. Many organic contracts provide that a contract will terminate if a breach “remains uncured” for a certain number of days. Often, a cure provision will be stated together with termination language.

Example: Intertwined Blanket Breach Termination and Cure Provision

Default, Breach: Each party may terminate this Agreement if the other party breaches any part of this Contract. If the breach is capable of cure, the breaching party must cure the breach within 14 days. If the breaching party fails to cure, termination is effective after the 14-day cure period expires.



It can be helpful to include contract language that describes some specific ways each party can cure specific broken contract promises. If you know exactly how to cure a breach, you can avoid disagreements about whether you have successfully cured a breach, and can be more certain to avoid breach or contract termination. Alternatively, the contract could require the buyer to notify you of a breach and describe the cure (if cure is possible). This kind of requirement would prevent a buyer from purposely failing to notify you of a breach until after the cure period had expired, effectively terminating the contract.



Example: Notice of Breach and Specific Cure Provision

In the event of breach, the non-breaching party must notify the breaching party of the breach within 48 hours. If the breach is capable of cure, the non-breaching party must also describe to the breaching party how the breach can be cured and a reasonable deadline by which any cure must be completed.

On the organic farmer's side, an example of cure could be removing a crop lien within a specified period or accepting a discounted price for low-quality deliveries (in lieu of total rejection). Curing a breach could also involve delivering a substitute product, delivering within a certain time frame, allowing access to records, or otherwise bringing your activities up to contract standards. For a buyer, cure could involve paying a penalty or premium price.

CHAPTER 5 – ENDNOTES

- ¹ Broiler chicken production contracts traditionally have guaranteed only one flock of birds delivered to the farm. Under a flock-to-flock contract, if a buyer decides to continue with a grower for a new flock, the same contract terms would remain in place for each subsequent flock delivered to the farm; but the buyer is free at any time to choose not to continue with the grower for any additional flocks. Some broiler contracts even state a time period for the contract, such as “three years” or “five years,” but do not guarantee delivery of more than one flock during that period. These contracts also often allow the company to end the contract at any time for any reason it chooses—even if the stated contract period has not ended.
- ² See 11 U.S.C. § 363(l), 365 (2012).
- ³ See 11 U.S.C. § 365(e)(1) (2012). This statute generally makes “termination upon bankruptcy” provisions unenforceable in so-called “executory contracts.” An executory contract is a contract where one or both parties have not fulfilled their obligations at the time of the bankruptcy filing. See also 11 U.S.C. § 541(c) (2012). A clause that terminates a contract because of the “insolvency” or “financial condition” of the debtor, or due to the filing of a bankruptcy case, will be unenforceable once a bankruptcy case has been filed. See, for example, Bob Eisenbach, *Are “Termination on Bankruptcy” Contract Clauses Enforceable?* (The Business Bankruptcy Blog, September 16, 2007), available at <http://bankruptcy.cooley.com/2007/09/articles/business-bankruptcy-issues/are-termination-on-bankruptcy-contract-clauses-enforceable/>.