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THE LEGAL DIMENSION OF CONTRACT FARMING

Promoting Good Contract Practices between Producers and Buyers in Contract Farming Operations in the Asian Context

BANGKOK, 26 September 2014

Report

OVERVIEW	2
• The Basics of Contract Farming	3
• The Forthcoming Legal Guide on Contract Farming	3
• The Consultation Workshop in Bangkok – 26 September 2014	4
SUMMARY OF PRESENTATIONS	5
• Welcoming and Opening Remarks	5
• Session 1: An Economic and Legal Introduction of Contract farming	6
• Session 2: The Legal Framework for Producer-Buyer Relationships – Country Overview	7
• Session 3: Practical Experiences – Contract Formation and Obligations of the Parties	9
• Session 4: Practical Experiences – Performance, non-performance and Dispute Resolution	11
• Closing Remarks	
SUMMARY OF DISCUSSIONS	13
• Scope, approach, purpose and form of the Guide	13
• Applicable legal regime and role of Government authorities in contract farming operations	13
• Parties to contract farming operations	14
• Negotiation and formation of contract farming arrangements	15
• Parties' obligations	15
• Non-performance situations	15
• Unforeseen events	16
• Dispute resolution methods	16
Annex I: Presentations	
Annex II: Program	
Annex III: List of participants	

Report on the Consultation Workshop
"The Legal Dimension of Contract Farming"
Bangkok, 26 September 2014

OVERVIEW

The Consultation Workshop took place at Century Park Hotel, Bangkok, on 26 September 2014, focusing on the legal aspects of the parties' agreement based on practical experiences and the treatment of contract farming in domestic legislation in the Southeast Asia region. This report summarizes the Workshop, entitled, "The Legal Dimension of Contract Farming, Promoting Good Contract Practices between Producers and Buyers in Contract Farming Operations in the Asian Context," which was organised by UNIDROIT,¹ in partnership with the Food and Agriculture Organization (FAO)² and the International Fund for Agricultural Development (IFAD).³ The Agricultural and Food Marketing Association for Asia and the Pacific (AFMA) was the organizing partner for the Workshop.⁴ In addition, the European Union provided support for the simultaneous interpretation English/Thai/English of the discussions, and as well as in funding the participation of a number of stakeholders' representatives.⁵

The Bangkok Consultation Workshop on contract farming was the second of a round of consultation events⁶ with stakeholders in contract farming relationships, primarily farmer communities and private sector representatives, in the process of preparing a UNIDROIT/FAO Legal Guide on Contract Farming. The Guide is currently being developed by UNIDROIT within a Working Group together with FAO and IFAD and the participation of other multilateral organisations.

¹ The International Institute for the Unification of Private Law (UNIDROIT) is an intergovernmental, Rome-based organisation specialising in the harmonisation and modernisation of private law rules at the global level, through international treaties and soft law instruments in various areas, including contract law.

² FAO will be co-authoring the Guide together with UNIDROIT and has provided support through the sharing of expert knowledge and the participation of delegations of experts providing comments and inputs on the drafts.

³ IFAD has also provided support through the sharing of expert knowledge and the participation of delegations of experts providing comments and inputs on the drafts. In addition, IFAD is providing substantial support to the preparation of the Guide through a grant to FAO (recipient).

⁴ With the support of international donors and in collaborating with international and national organizations, AFMA organizes workshop, training and manage project activities related to agricultural marketing. www.afmaasia.org

⁵ In Thailand, the EU is funding a project titled "Development of the Legal Mechanism for Protection the Farmer Right from the Contract Farming (DMFR)". Project staff and relevant key stakeholders were sponsored to participate in the consultation workshop in the framework of this project.

⁶ The first workshop of the consultation events took place in Buenos Aires (Argentina) on 25 March 2014, entitled "Contract Farming today, the right equilibrium", which was organised jointly by the World Farmers' Organisation (WFO) and UNIDROIT, with the cooperation of FAO and IFAD. WFO has participated as a key partner representing the professional and trade interests of farmers and has also provided support through the sharing of expert knowledge and the participation of delegations of experts providing comments and inputs on the drafts. The report of the first workshop is available in English at the following address: <http://www.unidroit.org/english/documents/2014/study80a/wg03/s-80a-wg03-18-e.pdf>.

The Basics of Contract Farming

An essential mechanism of the development and modernization of agriculture in industrialised countries over the past fifty years, the practice of producing under a contract has developed very significantly in many developing and emerging economies of the world. Most of today's agribusiness is organised in value chains, and at the bottom of these chains, more and more farmers produce under contracts with buyers. Virtually every commodity may be produced under contract farming, including crops, livestock, aquaculture and forestry – both for human and animal consumption as well as for industrial use.

Contract farming operations are based on an agreement, an "agricultural production contract," whereby an agricultural producer undertakes to engage in production and deliver at a future time goods meeting designated specifications, while the purchaser – typically a food processor, an exporter or a retailer – commits itself not only to acquire the product for an agreed price, but also to provide a certain level of control during the production process, typically by supplying inputs, technology or supervision.

From a contract law perspective, the agricultural production contract presents original features because it involves a variety of interlinked obligations on the parties (not only the parties to the contract but often also other participants in the value chain), and is approached in a variety of manners under domestic law. Under many legal systems, the production contract is subject to traditional legal categories such as a sale or a contract for services, while others recognise its *sui generis* nature, and yet others have developed a special contract type to regulate such contracts.

The Forthcoming Legal Guide on Contract Farming

In accordance with the authorization given by the Governing Council at its 91st session (Rome, 7 to 9 May 2012), the Secretary General of UNIDROIT set up a Working Group for the preparation of a Legal Guide on Contract Farming composed of contract law experts representing different jurisdictions and legal backgrounds, relying also upon the active cooperation of partner multilateral organisations and including an appropriate representation of agricultural producers and of the private sector. The Working Group is placed under the chairmanship of Professor Henry Gabriel (Elon University School of Law, Greensboro, USA), member of the UNIDROIT Governing Council.

The forthcoming Legal Guide has three broad objectives. First, it will provide a legal analysis of the type of arrangement upon which the contract farming relationship is based, as well as information and advice on good contract practices with a view to promoting the legal empowerment of agricultural producers during the negotiation and drafting of contracts. Second, the Guide also aims at providing advice for law makers and public authorities dealing at a public policy level with contract farming, in particular in the context of law reform. Last, the Guide is intended to serve as an additional tool available to international organisations and bilateral cooperation agencies, as well as nongovernmental organisations and farmers' organisations, engaged in strategies and capacity building programs in support of contract farming, especially in developing countries.

Accordingly, the Guide will describe common contract terms and discuss legal issues and critical problems that may arise under a variety of situations; analyse substantive law issues and identify problem areas and possible solutions in light of current trade usages and legislation; and provide guidance in the form of an internationally-recognised benchmark for assessing the fairness and overall balance of contract practices and relevant public policy instruments.

The Consultation Workshop in Bangkok – 26 September 2014

The workshop had the following objectives: promoting awareness and understanding of the economic, social and legal dimensions of contract farming (Session 1); discussing the diversity of approaches in the legal framework of domestic legislation of several countries in the Southeast Asia region applicable to contract relations between producers and buyers (Session 2); sharing stakeholders' experiences, recommendations, and best practices focusing on issues related to the negotiation process, the conclusion of the contract and the definition of reciprocal contractual obligations (Session 3); sharing experiences, recommendations, and best practices related to performance of parties' obligations, as well as non-performance and dispute resolution (Session 4); informing the content, scope, and purpose of the forthcoming Unidroit/FAO Legal Guide on Contract Farming with the inputs and discussions of the workshop. This and future consultation rounds will also explore the future use of the Guide and serve to build a network within target groups that will participate in the future implementation of the Guide.

Participants: The workshop was primarily addressed to a broad audience of stakeholders in contract farming relationships in the Southeast Asia region, *i.e.* producer organizations, private sector representatives, IGOs and development agencies, NGOs, public entities and the legal academic circles. Altogether, nearly 70 persons participated in the workshop.

Speakers included representatives of stakeholders and multilateral organizations (UNIDROIT, FAO and IFAD), as well as law professors and practitioners from different countries, particularly from the Southeast Asia region.

Material: The following documents were provided at the meeting:

- A project flyer, a leaflet on the Workshop, and the full-fledged programme prepared by UNIDROIT (in English and Thai). The final programme (in English) is attached in Annex II.⁷
- An abstract of the future Guide with an executive summary of chapters as a basis for discussion at the Workshop. The abstract document is accessible on Unidroit webpage as "Abstract document of the future UNIDROIT/FAO Legal Guide on Contract Farming."⁸
- A selection of informational material on contract farming, reference documents, and sample issues for consideration and resource materials on contract farming and the work of international partners, were made available to the participants through the event website⁹ and in soft and/or hard copy at the Workshop.

Languages: Documents and simultaneous interpretation at the Workshop were provided in English and Thai.¹⁰

⁷ Also available on the UNIDROIT Webpage at:
<http://www.unidroit.org/english/documents/2014/study80a/meetings/20140926-bangkok-unidroit-fao/programme-e.pdf>

⁸ <http://www.unidroit.org/english/documents/2014/study80a/meetings/20140926-bangkok-unidroit-fao/abstract-e.pdf>

⁹ <http://www.unidroit.org/work-in-progress-studies/current-studies/contract-farming>

¹⁰ Simultaneous interpretation was provided with the kind support of the European Union.

SUMMARY OF PRESENTATIONS

Welcoming and Opening Remarks

Mr Olan Pituck (*Director General, Department of Agricultural Extension, Ministry of Agriculture and Cooperatives of Thailand*) on behalf of the Department of Agricultural Extension, Ministry of Agriculture and Cooperatives of Thailand, extended a warm welcome to organizers and participants. Contract farming shall be regarded as a “two-sided coin,” in which both parties shall follow their commitments in order to reach a “win-win” situation. However, if any of the parties breach the contract, legal action shall then be taken. In Thailand, there is no specific law on contract farming. When problems occur, parties tend to solve it through negotiation and compromise. The workshop shall offer an important platform for stakeholders to share experiences and views on the content of the Legal Guide on Contract Farming. Mr Pituck emphasized that the Department of Agricultural Extension has a long experience to promote contract farming through providing analysis of suitable locations, training farmer groups, acting as an intermediary for contracting, and transferring technology for problem solving. He provided one case study example of a successful contract farming scheme in the western region of Thailand involving a Japanese buyer and other exporting companies which has been supported by the Department of Agricultural Extension. Mr Pituck expressed his belief that the outcome of this workshop will be highly constructive for all stakeholders.

Mr Hiroyuki Konuma (*Assistant Director General and Regional Representative for Asia and the Pacific Food and Agriculture Organization of the United Nations - FAO*) thanked the Department of Agricultural Extension of the Ministry of Agriculture of Thailand for hosting this event, UNIDROIT for organizing and IFAD for supporting the Workshop, as well as all participants. The core theme of this workshop, contract farming, is given a high priority on the agenda of most countries in the Asia-Pacific, a region representing around 70 percent of smallholder farmers in the world. The region is facing new challenges as its population continues to grow, and farmers are still facing difficulties when it comes to access to inputs, markets, and modern technology. New trends are arising consequently, including new dietary patterns, living conditions, and daily habits. Such shifts are driven by the region’s fast economic growth. Changes in dietary habits also create new demands in intangible food attributes related to safety, quality, diversity, and supply regularity. Demand for non-grains and processed foods is also increasing, while demand for certain grains, such as rice, is decreasing instead, especially in middle-income countries. To address those issues, responsible contract farming is one of the mechanisms that can help to improve efficiency and inclusiveness in transforming the food and agriculture system.

Mr Benoit Thierry (*Country Program Manager, International Fund for Agricultural Development - IFAD*) welcome all participants. He reminded participants of IFAD’s role in supporting agriculture related activities based on its mandate in poverty alleviation. An international finance institution, IFAD provides loans to governments, helping governments to implement new policies to promote agriculture with smallholder farmers. IFAD strongly supports agricultural schemes based on contract farming, which is seen as an interesting tool to reduce poverty and to bridge the gap between traditional agriculture and markets, thus providing a better income to smallholders. Mr Thierry emphasized that Asia could inspire the rest of the world for bringing small farmers into the markets, showing that a wealthy agriculture model based on smallholders is possible. He emphasized the importance of ensuring fair contracting, especially in view of the vulnerability of some farmers, and of taking into account the cultural aspects of the particular situation. He reminded that ensuring that consumers receive better quality products and offering producers fair prices and sustainable practices are two key elements which will make contract farming a win-win operation.

Mr Henry D. Gabriel (*Professor of Law, School of Law, Elon University (USA), UNIDROIT Governing Council Member, Chairman of the UNIDROIT Working Group on Contract Farming*) also welcomed workshop participants. He emphasised the importance of the workshop outputs for the process of drafting of the UNIDROIT/FAO *Legal Guide on Contract Farming*, by gathering experts from different countries to discuss practical experiences, to make policy recommendations, and to address current problems in contract farming in the Asian context. The Guide is expected to become an internationally recognized legal reference, with a fair and balanced approach against which contract practices and public policies can be assessed. Contract farming contributes to provide several benefits for developing production sectors, including the formation of capital, technology transfer, and to increase production yields, but it may also carry several risks that the Guide will try to address. The Guide will in particular enhance the ability of the parties to establish a stable and fair relationship, based on a balanced contract, which is the cornerstone of the relationship, helping the parties to outreach difficulties, to distribute benefits fairly, and to build a predictable environment.

Session 1: An Economic and Legal Introduction to Contract farming

Mr Carlos A. da Silva (*Senior Agribusiness Economist, Rural Infrastructure and Agro-Industries Division, Food and Agriculture Organization of the United Nations, FAO*) presented on "Contract farming and inclusive value chain development." Contract farming has the potential to promote more efficient agricultural supply chains and the economic and social inclusion of smallholders. The concept of "smallholder" itself is difficult to define as it depends on characteristics of each country, but smallholders represent the vast majority of farmers around the world. Due to their geographical dispersion, lack of organisation and access to services, marketing of small volumes, there are challenges for the inclusion of smallholders. In its mission, the FAO tries to address these issues by linking farmers to markets under different approaches. Contract farming is not a new concept, but interest in contract farming has been renewed, because agri-food systems are being reshaped and supply chains modernized, focusing more on corporate responsibility in order to promote contractor business models. In discussing the role of contract farming for inclusive market access, he emphasized that expansion of contract farming will not necessarily lead to exclusion of smallholders from agri-food supply chains, as there many others factors that can play a role in the selection of suppliers. Moreover, there is a trend of convergence in clauses and conditions in contracting operations, despite commodity differences. Also, major problems, such as side selling, are inevitable, but operators shall make it manageable. A contract farming planning strategy is a key of success for the relationship. Mr da Silva recommended that the Guide being developed should aim to promote trust building rather than confrontation.

Mr Henry D. Gabriel (*Chairman of the UNIDROIT Working Group on Contract Farming*) presented the forthcoming UNIDROIT/FAO *Legal Guide on Contract Farming*. The Guide is structured as a commercial code, in that contract farming is a sub-sector of commercial law. Contracts in contract farming operations may be classified into different categories depending on the underlying relationship. As it is impossible to introduce each type of specific contract, the Guide will address general legal principles of contract law, including the rules of the governing law, either based on express terms of the agreement or on specific legislation requirements, reminding that there are potentially different types of sources depending on the legal traditions, civil law or common law. While illustrating the variety of approaches under specific pieces of legislations, the Guide will not go beyond general principles, in a number of areas of the contractual framework, including the supply of inputs, contract duration, terms of payment, quantity and quality requirements, liability of inputs, risk of loss in general, contract termination, and dispute resolution. The Guide is intended to be used by its three primary

audiences: parties involved in contract farming, governments that would rely on a guide for future legislation and policy information, and development agencies that are involved in contract farming promotion.

Session 2: The Legal Framework for Producer-Buyer Relationships – Country Overview

Mr Virgilio R. de los Reyes (*Secretary, Department of Agrarian Reform, Quezon City, Philippines*) started by noting that in the inception stage of a business contract relationship, certain issues are critical regarding the bargaining power of farmers, in particular the type of legal entity involved in the production, the nature of rights over the land, the general lack of access to information and to credit support. Applicable rules for contract farming in the Philippines are sourced from the Civil Code and other relevant laws. The Philippines adopted special legislation in 2006 (Dar Administrative Order No. 09-06 governing Agribusiness Venture Arrangements (AVAs) in Agrarian Reform Areas) which aims at guaranteeing security of land ownership and tenure and of an increased income for the beneficiaries of agrarian reforms. The Act grants the Government extensive powers in the creation of contract farming agreements, through contract review and approval procedures (such as regarding the economic viability and profitability of the contract) and in the monitoring of contract implementation and in dispute resolution. However, concerns regarding the effective ability of the Act to reach the expected objectives provide major grounds for considering legislative reforms. Mr de los Reyes emphasized that a number of policy questions must be considered surrounding the contract farming arrangement, and that consideration should be given to how best to protect farmers and increase their bargaining power without overregulating contract farming operations. He referred to the important role of standards enshrined in guidance instruments developed by international organizations such as the Voluntary Guidelines of Land Tenure and the draft Principles of Responsible Agricultural Investment (PRAI), as well as the forthcoming UNIDROIT/FAO Legal Guide on Contract Farming.

Ms Lawan Thanadsillapakul (*Professor of Law, Sukhothai Thammathirat Open University, Thailand*) reported that the nature of contract farming is difficult to determine in Thailand. There are no specific laws nor a suitable regime in Thailand for contract farming. Because contract farming agreements involve several elements, Thailand's jurisprudence considers that the regimes applicable to sales contracts, labour contracts or service contracts are not suitable. Although serious issues may derive from the lack of bargaining power held by the farmer, legislation regarding unfair terms is also regarded as not applicable. This situation could have negative impacts, especially when the buyer is providing inputs at an unfair price, resulting problematic indebtedness for farmers. In order to remedy to this situation, standard contracts have been introduced by government agencies; but, this practice has failed as it was seen as an attempt to over-regulate the sector. Finally, Ms Thanadsillapakul addressed the main concerns that the Legal Guide is expected to solve: first, conditions for balancing the bargaining power between farmers and buyers; then, to define mechanisms to guarantee the price of agricultural products and market access for farmers; and also, to recommend an adapted dispute resolution mechanism.

Mr Paripurna P Sugarda (*Professor of Law, University of Gadjah Mada Faculty of Law Yogyakarta, Indonesia; Member of the UNIDROIT Working Group on Contract Farming*) emphasized the prevalence of smallholders and traditional communities of agricultural producers involved in contract farming relationships and the strong impact of the social and cultural dimension in most contract farming operations. Prof. Sugarda indicated that although no special legislation on contract farming is applicable in Indonesia, customary law may be

relevant, which is expressly included among the applicable legal sources by the Indonesian Constitution. Customary law focuses on principles of community (especially community-based ownership of land) and family systems. The cooperative system is also enshrined to design the development of the national economy. Agricultural production is rooted in traditional systems for producers and their families with a major impact on the life of the producers and their families, an aspect which should be taken into account by contractors whose activities are based on business principles. When contracting with companies, farmers are vulnerable, and a relationship that should be fair in theory is often unbalanced in practice. In this context, the concepts of good faith and fair dealing are important, and trust should be developed from the very beginning. Very often contracts are informal or unwritten, and many factors may worsen the producer's position during the implementation of the contract with potential human rights and environmental issues. Adverse conditions include in particular the weakness of law enforcement, and dispute resolution costs.

Mr Prasnar Yi (*Lecturer of Law, Royal University of Law and Economics (RULE); President of Henri Capitant Friends of Cambodian Law Association, Cambodia*) indicated that the legal framework for contract farming in Cambodia is formed of a variety of potentially relevant legal sources. Cambodia adopted a Sub-Decree in February 2011 which regulates "contract-based agricultural production." This regulation sets formal requirements for the formation of contracts, states minimum contract content regarding parties' obligations and requires that disputes be solved through amicable procedures, if need be under the authority of a government entity. Other pieces of legislation dealing with producer organizations and land management may also be relevant. In addition, the general principles of contract law provided by the Civil Code are applicable to all issues which are not covered by the special regulation, including in relation with issues of formation, performance and non-performance as well as termination of the contract. General principles are also relevant such as the concepts of good faith, abuse of rights, freedom to contract and parties' autonomy. Provisions regarding the validity of contract, in particular the prohibition of taking unfair advantage of the other party's weakness, or the need to comply with public order and good morals may be particularly relevant in the context of contract farming relationships. Also, provisions dealing with force majeure are relevant, although this concept still lacks precise boundaries in its practical application. Finally, other legal sources may be relevant in dealing with the series of contracts around the contract farming relationship and with particular aspects involved in contract farming relationships such as labour law and insurance law.

Dr Dang Kim Khoi (*Center for Agricultural Policy, Institute of Policy and Strategy for Agricultural and Rural Development – IPSARD Hanoi, Vietnam*) presented a review of policies related to contract farming in Vietnam, pointing out some problems and providing policy recommendations. Although the concept of and legal framework for contract farming have existed in the nation since 1981, currently there are few policies related to this practice, though including the Civil Code 2005, Decision 62/2013/BNNPTNT, and Circular 15/2014/TT-BNNPTNT. While the former stipulates a general reference of various contracts, the two latter documents promote the implementation of contract farming between smallholders and entrepreneurs in large-field production projects. These two documents aim at supporting (i) the horizontal linkage between smallholders to achieve 'the economy of scale' effects: reducing production and transaction costs, increasing capacity to access new technology and market, strengthening bargaining power and competitiveness, and reducing risk and (ii) the vertical linkage between farmers and entrepreneurs to build up a new value chain with higher quality and a smaller number of actors. Nevertheless, in reality, this policy framework creates some problems. First, its strict regulations regarding criteria of large-field production zones and investment in infrastructure prevent a number of entrepreneurs from participating in contract farming. Second, this does not provide an effective mechanism to prevent contract

breach. Third, this framework seemingly ignores the promotion of agricultural contracting between smallholders and entrepreneurs who are not eligible for large-scale production projects. The presentation ended by providing some policy suggestions related to production zone planning, common production procedure consolidation, legal training for related parties, contract price determination, product's quality and safety, mediation institutions, and promotion of contract farming activities of smallholders and entrepreneurs who are not eligible for large-scale production projects.

Session 3: Practical Experiences – Contract Formation and Obligations of the Parties

Mr Ubol Yoowah (*Vice Chairperson, Community of Agro-Ecology Foundation – CAEF Thailand*) presented three particular examples of possible severe consequences of certain contract farming operations in Thailand. In the first case, following the bankruptcy of the contractor in the poultry industry, a significant number of producers suffered high losses. The case was pending before the bankruptcy court, but the outcome was likely to be that the farmers will receive no or very little compensation, as other creditors (banking institutions) would have priority in the settlement of the bankruptcy. In the second case, producers had given their lands as collateral to obtain finance from a banking institution to invest in the necessary equipment for the poultry production. The contractor went bankrupt, and as a result the producers were not able to repay the bank loans and the bank enforced the guarantee clause and put the lands on auction. The third case referred to different practices aiming at weakening the farmers' position. In certain situations, contractors would use patronage mechanisms, consisting for the contractor in taking care of the producer's family and having the producer working for free. In some other cases, the contractor may select the chief of the village as a representative of the company, obligating farmers to act accordingly to the directives of the chief of the village. Finally, Mr Yoowah discussed the fact that the current legal framework does not provide any dispute resolution mechanism or effective remedies. For those reasons, CAEF, supported by academic institutions and different stakeholders, is promoting a project of a law on contract farming which seeks to address such issues.

Mr Sok Sarang (*National Team Leader of Component #3 on Contract Farming; Support to the Commercialization of Cambodian Rice Project (SCCRP); Cambodian Institute for Research and Rural Development - CIRD Cambodia*) presented SCCR, a pilot project funded by the French Agency for Development (AFD), and supported by the Department of Agro-Industry of the Ministry of Agriculture, Forestry and Fisheries (DAI-MAFF) under the Sub-decree 36 of 2011. MAFF is the main facilitator in the contract formation process and is also in charge of monitoring and evaluating contracts between buyers and producer organisations and cooperatives, and as necessary also in conflict resolution. Based on the project, a contract template has been put in place dealing with the following terms: object, duration, rights and duties of the producer, rights and duties of the buyer, harvest and transportation, determination of product quality, price, payment, disasters, termination of contract, conflict resolution, development of the contract and language clauses. Mr Sok highlighted the fact that challenges still remain for a full implementation of the regulation on contract farming. First, cultural change in the public administration is needed to develop service and cost efficiency rather than control and imposition of heavy procedures. Then, more incentives shall be provided to encourage parties to enter into contract farming agreements, which can be used as a tool in support of public policy objectives. Finally, with a view to enhancing the confidence of the parties and security in contract farming, it is recommended to develop contract enforcement mechanisms, in particular through arbitration proceedings and the enforcement of arbitration decisions. Finally, an important challenge is to cover risks that are out of the

control of both parties (climate or pest risks, notably), possibly through the development of crop insurance schemes.

Mr Jude A. Andrada (*Head, Accounts Management and Development Group, National Livelihood Development Corporation (NLDC), Philippines*) presented the Farmer Entrepreneurship Program (FEP) which was conceptualized and implemented by NLDC, a government owned corporation, together with an international NGO and a foundation of the biggest local food chain company in the Philippines. The program is currently being implemented in several sites throughout the Philippines, involving farmers producing various crops, which are being directly supplied to institutional markets. Marketing agreements with buyers are negotiated and contracted directly by the farmer's associations themselves with supervision and monitoring being provided by a working group composed of representatives from the partner institutions. Legal documents or marketing agreements are in various forms, including electronic communication based on e-commerce law. Mr Andrada recommended that any legal agreements should be simple and preferably in the local dialect, because the farmers are generally uncomfortable with formal agreements. It is also deemed necessary that the buyers provide technical assistance to the farmers, and price may be renegotiated if lower than market price. For this program, the Microfinance Institution and the farmers basically share the risk, but the establishment of an Agricultural Guarantee Fund could help to reduce the risks. Some conclusions and recommendations can be drawn from the Program's implementation and experience that can strengthen contract farming arrangements, improve value chain linkages and help ensure that business transactions are transparent, fair, and viable for both parties - the producer and buyer. Ultimately, the program envisions shaping the mind-set of farmers to become entrepreneurs, managing sustainable agro-enterprises and improving their socio-economic conditions.

Mr Andrew Cockburn (*Sadhana Arifnusa Corporation, Indonesia*) shared his experience on the way the private sector interacts with farmers and how the private sector may contribute to agricultural diversification in Indonesia. Sadhana Arifnusa Corporation is involved in growing different types of crops, managing 22,000 farmers in Indonesia, with more or less intensive levels of management, but always providing technical inputs and access to market. The business model of the Company has been renewed and it is now based on the concept of "mixed-farming," switching from a single-crop (tobacco) to a more comprehensive agricultural company, which grows maize, soybeans, rice, livestock, with some activities in forestry. In a case study, Mr Cockburn tried to demonstrate the ability of farmers to diversify their production when they receive necessary support from the private contractor and when the relationship is based on a contract farming management plan under a long-term approach. He also emphasized the fact that farmers are the company's greater assets. In this regard, farmers are allowed to choose the type of their production and keep freedom to turn over another type of crop, thus giving them flexibility to diversify their sources of income. Within this approach, Mr Cockburn considered that there is no need to over-regulate contract farming operations. Regulation made by people outside the business may not be adapted to different approaches of contract farming, and may restrain investment in small-scale farming, worsening the current situation in which the younger generation is reluctant to engage in agriculture. On the other hand, supportive regulation could help farmers, at the local level, to overcome situations that are beyond their control.

Mr Souvanthong Namvong (*Deputy Head of Training Section, Department of Agriculture Extension and Cooperatives Ministry of Agriculture and Forestry Vientiane, Lao PDR*) presented the general framework of contract farming in Lao PDR in the context of the transition from subsistence agriculture to an industrial model. There are two categories of agricultural production in Laos: first, agricultural production based on formal agreements (contract

farming or land concession); second, informal arrangements. The role of local authorities as facilitator is important, especially at the village level, for giving to parties the opportunity for open dialogue and negotiation, for providing information and advice to farmers regarding advantages and risks involved in a contract farming relationship, for facilitating the purchase of inputs and exportation of the production, and for monitoring the enforcement of the contract. Foreign agricultural companies involved in contract farming production in Laos must receive approval by the authorities. In practice, there are disparities regarding the share of liability. On the part where foreign companies are operating, companies choose to bear production loss; while in other parts where local stakeholders are involved, losses are shared by the parties. There are two categories of dispute settlement: "informal" and "semi-formal," including mediation by village authorities and mediation by third-parties; and, formal proceedings that are not generally used in practice.

Session 4: Practical Experiences – Performance, Non-performance and Dispute Resolution

Mr Antonio Salvador (*Legal Consultant, Asian Farmers Association – AFA, Philippines*) presented the findings of a study conducted by the Initiatives for Dialogue and Empowerment through Alternative Legal Services (IDEALS) on contracts involving banana growers in Mindanao, Philippines. While many provisions of the various studied contracts were regular and even beneficial to all parties concerned, some contractual terms were highly questionable. Prices paid to farmers are low, even as inputs are charged to them by the corporations, albeit without the benefit of informed judgment and prior consent. Also, risks of rejection by the buyers abroad are unjustly passed on to the farmers, even after the corporations had already assumed possession and ownership of the produce. However the farmers are not given their fair share when the corporations benefit from an increase in prices. Two factors are considered to be the main reasons to keep the prices low. First, even though the domestic regulation requires that the price shall be indicated in the agreement, there are no guidelines about the determination of a fair price. The lack of reliable information on fair market prices is also a constraint. Second, the price review mechanism provided by the legislation is ineffective in practice because of its contractual nature. There is also a vacuum with respect to dispute resolution mechanisms. Producers are forced to file cases to invoke a breach of contract, but this remedy is left unused because farmers cannot afford to bear the cost of litigation. Mr Salvador emphasized that this situation is favourable to draw farmers in debt. In order to ameliorate the contracting partnership, he issued several recommendations, including the establishment of proper access to information; the establishment of a business climate built on conditions of fairness; and, the need to provide regular training and support to farmers.

Mr Hamid Bin Sulaiman (*Head of Transformation Department, National Farmers Organization (NAFAS), Malaysia*) presented the objective and practices of NAFAS to improve agricultural production in Malaysia through contract farming. NAFAS, as a private and social company, gathers farmer organizations at the national level and local level. NAFAS also acts as the integrator and has poultry production contracts with farmers, coordinating the production. The missions of NAFAS are to improve agricultural development, improve farmers' knowledge and skills, increase farmer's revenue and income, and improve the socio-economic development of farmers. For that, NAFAS uses contract farming based on an integrated value chain aiming to increase income and make it sustainable for farmers, and to secure supply for the buyers, guaranteeing consistent supply and quality of the products based on a specific food certification.

Ms Mattana Gosoomp (*Co-founder of Sustainable Alternative Development Association - SADA, Thailand*) presented the activities of SADA to promote justice and fair practices in the

contract farming system in Thailand. This project gathers stakeholders from different institutions as implementing partners: academic institutes, farmer-producers, NGOs, GOs and also the Law Reform Commission of Thailand. Activities are focusing on capacity building of the farmer community and policy advocacy on the concept of “Healthier and Better-Contract Farming,” with a special focus on linking farmers and government agencies. Ms Gosoomp emphasized the fact that working with different ministries contributes to forging more efficiently the path toward a fair mechanism in contract farming. Currently, the legal framework of contract farming in Thailand is uncertain. The unbalanced situation between farmers and buyers is often brought about before the signature of the contract. Farmers are often asked, as a precondition, to handle the preparation of infrastructure by contracting bank loans and using their own land or property as collateral. Under such situations, farmers may lack bargaining power when it comes to price determination of the products or inputs. Also, in case of a natural disasters which are recognized by the official authorities, farmers are often asked to allocate in priority the compensation amount to the contractor for the compensation of the loss.

Mr Tran Quoc Dat (*Deputy General Director, Hiep Tai Food Company Ltd, Vietnam*) presented dispute resolution under a legal and practical viewpoint in Vietnam. Dispute settlement bodies may be divided into two categories: bodies issuing binding decisions (judicial or arbitration courts); and, bodies issuing non-binding decisions. Generally, judicial courts are preferred to settle disputes, but although the court fees are low, the legal proceedings may last for years. Commercial arbitration is a reality in Vietnam, but it is not a common way to settle disputes related to contract farming because of the cost of the procedures. Mediation and negotiation may also be a way to settle dispute without having a binding decision. Due to the lack of experience and knowledge of bodies in charge of the mediation in solving dispute involving high-value contracts, it may be needed to create a special jurisdiction to handle such dispute. The non-performance of the contract may result in different types of remedies: compensation for the material damages/loss, penalty, order to stop the breach behaviours and continue to implement the contract, the termination of the contract, to stop contracting with the producing party for further production or even the cancel of the incentives provided.

Mr Yi Bunhak (*Chief of Development Agro-Industry Office/DAI Ministry of Agriculture, Fisheries and Forestry, Cambodia*) dispute resolution under a legal and practical viewpoint in Cambodia. He noted that before the entry into force of the new regulation in 2012, most contract farming projects had failed mainly because of side selling and the lack of law enforcement. Although local authorities played a role in conflict resolution as facilitator, parties were more willing to file their claims to the courts due to the lack of knowledge of the facilitators in agricultural matters. However, the costs involved in judicial proceedings have contributed to discourage investors from entering into contract farming operations in Cambodia. The new 2012 regulation sets a specific conflict settlement mechanism handled by the Ministry of Agriculture and an inter-ministerial committee. Finally, Mr Bunhak discussed the fact that, until now, private sector investors remain reluctant to engage in contract farming because of the burden of administrative procedures, and thus recommended that the government should take appropriate measures to provide more incentives to attract investors.

CLOSING REMARKS

Mr Henry D. Gabriel (*Chairman of the UNIDROIT Working Group on Contract Farming*) addressed his congratulations to all speakers and participants for contributing to provide tremendous information and experiences. On behalf of UNIDROIT, he expressed his deepest appreciation to participants. He emphasized the fact that the importance of contract farming in

Asia is reflected by the participation from various organizations to this event. The discussion provided shall not only be considered as an output that will inform the content of the final version of the *Legal Guide on Contract Farming*, but shall also be regarded as an important amount of knowledge collected by everyone for the purpose of dissemination within participants' operating environment.

SUMMARY OF DISCUSSIONS

The elements reported in this section are organized by subject matter and reflect the exchanges among panel members and workshop participants during the workshop on 26 September 2014.

Scope, approach, purpose and form of the Guide

- As regards policy approach toward contract farming regulation, it was noted that the various interventions in Session 2 provided a telling illustration of the diversity of approaches among different domestic legal systems of the region. It was important to remind that the forthcoming UNIDROIT/FAO Guide would not make recommendations in this regard. It would rather describe how agreed contract terms and mandatory provisions of the applicable law could influence the balance of the contract, an approach that could be helpful for Governments to take into account in the process of considering the adoption of a piece of legislation which would apply to contract farming relationships.
- A central objective of the Guide was to promote economically profitable operations both for the producer and for the buyer/contractor, recognizing that both parties should find a commercial interest in the successful outcome of the contract. The drafters of the Guide have been at all times mindful of the balance and the win-win situation that must be achieved. This has been reflected in the elaboration process, aimed at taking into consideration the concerns expressed by all stakeholders. While the regional consultations in Buenos Aires, Bangkok and Addis Ababa provided an opportunity to come close to the agricultural producers' concerns, the public consultation on the draft version of the Guide through the Internet and the organization of a consultation particularly targeting the private sector would enable the drafters to fully include the industry's viewpoint.

Applicable legal regime and role of Government authorities in contract farming operations

- The question of the determination of the applicable legal regime for contract farming operations may be unresolved in certain jurisdictions. Parties may be engaged in contract farming operations which have operated under an unspecified regime, leading to legal insecurity.
- While in some countries, contract farming arrangements would fall under the sole general contract law regime, other countries have put in place special regulations in the context of targeted public economic and social policies.

- It was suggested that the idea to establish the support fund to reduce the risk for both farmers and buyers as presented by Mr. Andrada should be translated into concrete action.
- It was noted that support from a public authority under a particular regulation may be conditional upon specific requirements (size of the production zone, investment in infrastructure), but this would not prevent parties from entering into a contract farming arrangement not subject to the regulation, in which case they would not be eligible for the corresponding support or incentives.
- In presenting the role and modalities of Government intervention in contract farming operations for economic and social public policy objectives, participants referred also to the complex procedures involved when such intervention is directed toward every single contract in all its stages, the efficiency problems and cost implications which often constitute a major impediment to a successful implementation of the regulation, and an adequate environment for parties to develop activities.
- It was noted that in the context of the ASEAN Economic Community (AEC) to be implemented in 2015, contract farming operations would certainly be impacted by the liberalization of investments at the regional level in the agriculture sector. Such liberalization may have an impact on the change of size of investors, as it will facilitate the expansion of local investors at a regional level. It will also become more attractive for foreign investors in the agribusiness industry to establish in an ASEAN country to have access to the regional market. It was noted that free-trade agreements covering contract farming arrangements were already in force between certain ASEAN countries. It was suggested that the Legal Guide should also take into consideration such situations which may impact on the balance of individual relationships between contractors/investor and farmers.
- Regarding the potential role of Government, it was suggested that during the contract formation and negotiation stage, farmers in developing countries, due to their lack of ability to hire lawyers, should be provided assistance in terms of legal advice on what the provisions of the proposed contract mean. This should consist in simply informing them of the implications and possible interpretation of the contract. The farmers themselves would have to decide after receiving such information. This could be important to prevent the inclusion of provisions in the contract which are onerous and disadvantageous to the farmers. In response to the suggestion, it was mentioned towards the end that the question is who will do it (the government, NGOs, lawyers, etc.).

Parties to contract farming operations

- It was noted that “farmers” referred to a constellation of people, not only by size, by commodity, by particular geographic area. The complexity and diversity of situations should be taken into account.
- The legislation may require that farmers should be a member of a registered cooperative to have the capacity to become a party to a production contract. Special attention was drawn on the impact it could generate on the taxation regime, resulting on heavy taxation to be borne by individual farmers. Some legislations do not provide a special legal regime for the establishment of farmers groups. It was noted that cooperatives and farmer associations might play an important role in credit management, as well as suggest that legislation may include small and micro community enterprises.

- Government agencies may also provide support to local authorities without interfering into the negotiation between the farmers or farmers group and the buyers. The role of third parties, including public authorities or non-profit organizations, in providing assistance in building of legal and negotiation capacities for farmers was repeatedly emphasized. It was remarked that the private sector might also be involved in supporting the establishment of farmer associations.

Negotiation and formation of contract farming arrangements

- Before the contract is signed, it may be required by the applicable regulation that parties submit the content of the contract for prior review and approval by an official authority.
- Based on local practices, prior to the formation of the contract, parties may invite a representative of the local authorities to sign the contract as a witness.
- But local authorities are not always involved, neither in the process of formation of the contract, nor during the implementation phase. Contract farming arrangements shall then be formed by the mere exchange of consent between the parties, under the general principle of the binding effect of agreements (principle of *pacta sunt servanda*)

Parties' obligations

- Even though the need for using the contract as a legal tool to define parties' respective obligations was not contested, the fact that "trust" shall be given a priority was repeatedly emphasized. In several cases, sustainability of the relationship based on individual understanding and mutual commitments showed that it improved the return on investments while contributing to improve farmers' living environment.
- Successful relationships result from good deals offered to farmers, with very low levels of default, in particular side-selling.
- In order to secure the investment made by the farmers, legislation may require that the buyer shall provide, prior to the formation of the contract, a certain percentage of the total amount of the production to a fund to guarantee the farmers in case of non-performance.

Non-performance situations

- Informality is a common way of dealing with non-performance situations. In many cases, this would enable a sharing of risks. The example was provided where large buyers with multiple suppliers would be tolerant in case of farmers' default. According to one opinion, the parties shall adopt an approach focusing on fairness in accepting to share liability of their respective loss.
- Such approach shall not minimize the role of lawyers in designing the agreement between the parties. It was noted that, even if the Asian context, the contract shall play a role in managing the expectations of each parties.
- Contractor's default was seen as a major risk for farmers. Facing this situation for farmers would be even more difficult when they have contracted a loan – including in many cases by giving out the land as collateral - to finance the production and are no longer in a position to reimburse the loan. In the particular situation when the contrac-

tor is bankrupt, obtaining payment in the bankruptcy procedure may be challenging especially when other parties would have priority ranking in the liquidation of the contractor's assets. It was recommended that the Guide should present the variety of mechanisms that are available in certain jurisdictions to protect the producers in such circumstances, such as security funds or possible priority rights for the farmers. The example was given in one jurisdiction of the obligation imposed upon the buyer to make a guarantee deposit prior to the production in the amount of 10-15%.

- Several examples of unfair or abusive situations were mentioned. One referred to relationships whereby the contractor would provide support to the farmers' family but no financial remuneration to the farmer. It was also indicated that unfair practices may be reflected in the obligation for the farmers to finance the preparation of infrastructure before entering into the production contract with the contractor.

Unforeseen events

- The discussion on unforeseen events mostly focused on the consequences of natural disasters – such as floods or animal disease which are frequent in the Asian region – resulting in the loss of the production before it is delivered to the contractor. Based on general legal provisions, natural disasters should be regarded as a case of *force majeure* releasing the producer from its obligations. It was noted that in some jurisdictions, although the *force majeure* concept is provided for under the law, it is incompletely defined and lacks judicial interpretation or legal enforcement.
- Depending on the size of the farmer and the balance of bargaining power, liability for failure to perform the contract may be negotiated. Cases were reported where failure to perform as a result of natural disaster would be treated like a breach of contract by the producer. The *force majeure* exemption under the law would remain inoperative because farmers rarely bring the case to the court.
- The allocation of risks and liability may also be a contractual matter, and it was noted that in practice, solutions vary even within a single country. The example was reported that in certain areas, producers would be exempted from the obligation to deliver but would still have to repay the inputs provided by the contractor at the following harvest; in other areas, the foreign buyer would bear the loss, a situation which is explained by a more profitable market for the investor.
- The importance was illustrated in this context of relying on the advice of legally trained persons to draft the contract, as the *force majeure* clause may have a major impact on the balance of the contract. The forthcoming UNIDROIT/FAO would certainly provide useful guidance in this regard.
- Also several participants referred to the importance of mechanisms to cover risks that are out of the control of both parties (climate or pest risks, notably), such as insurance schemes or other mechanisms that work as security-net when events beyond the control of farmers/producers occur.
- Mention was made of the role that microcredit can play to support production activities, and the importance that microfinance institutions use guaranty fund and micro-insurance to minimize the risks for the farmers.

Dispute resolution methods

- The point was made that very often the legal framework does not provide adequate dispute resolution mechanisms and effective remedies.

- Some examples of legislation provide for dispute resolution mechanisms based upon an escalation principle, with progressive steps. The first level is based on parties' consent providing an alternative to judicial proceedings. The legislation may require that parties should have recourse to a mediation forum before turning to a binding dispute resolution mechanism. Legislation may also organize for dispute settlement boards, and in such case would parties would be entitled to file their claims to such bodies only if the public authorities have initially endorsed the contract farming arrangement.
- It was generally admitted that any effort to avoid litigation should be pursued, as judicial procedures are generally time-consuming and expensive. As a general principle, negotiation between the parties should be encouraged. Mediation offers an adequate mechanism in many cases, with a neutral third party helping parties to reach some sort of agreement, in many cases, the farmers' organizations or chambers, NGOs, etc.
- It was also pointed out that in certain contexts, arbitration may be adapted to contract farming: it is quick, it is affordable, and unlike going to court, the arbitrators usually have deep knowledge and understanding of the industry. The requirement of a neutral system of arbitration was particularly emphasized. Concerns have been raised that, usually, the party with the power to draft the contract tends to insert an arbitration clause with mandatory arbitration when this party is sure that the arbitration system is driven by the industry.
- Public authorities may be involved in the dispute resolution process. When there is a dispute, rather than going to the court, parties may approach the local authorities to enter into negotiation, and it may be efficient to reach a compromise.
- Reference was made to the possible establishment of specialized boards or authorities to solve dispute in contract farming, which had been put in place successfully for particular economic areas or industries in certain countries. Since such authorities are independent, to be sustainable they must rely on private funding.

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THE LEGAL DIMENSION OF CONTRACT FARMING

Promoting Good Contract Practices between Producers and Buyers in Contract Farming Operations in the Asian Context

BANGKOK, 26 September 2014

Annex I: Presentations

Mr. Olan Pituck
Mr Hiroyuki Konuma
Mr Benoit Thierry
Mr Henry D. Gabriel
Mr Carlos A. da Silva
Mr Henry D. Gabriel
Ms Lawan Thanadsillapakul
Hon. Virgilio R. de los Reyes
Mr Paripurna P. Sugarda
Mr Prasnar Yi
Dr Dang Kim Khoi
Mr Sok Sarang
Mr Jude A. Andrada
Mr Andrew Cockburn
Mr Souvanthong Namvong
Mr Antonio Salvador
Mr Ab Rahman Ismail
Ms Mattana Gosoomp
Mr Tran Quoc Dat
Mr Yi Bunhak
Mr Henry D. Gabriel

WELCOME AND OPENING SESSION

Mr. Olan Pituck

Director General, Department of Agricultural Extension

Mr. Hiroyuki Konuma, Assistant Director General and Regional Representative for Asia and the Pacific, Food and Agriculture Organization of the United Nations

Mr. Benoit Thierry, Representative from International Fund for Agricultural Development

Mr. Henry D. Gabriel, Professor of Law, School of Law, Elon University, UNIDROIT Governing Council Member, Chairman of the UNIDROIT Working Group on Contract Farming

Distinguished guests and participants,

Ladies and Gentlemen,

Good morning to you all.

I am delighted to welcome you all to the Workshop on Promoting Good Contract Practices between Producers and Buyers in Contract Farming Operations in the Asian Context, on behalf of agriculture division, Department of Agricultural Extension, Ministry of Agriculture and Cooperatives. You all know that this workshop is taking place for informing the drafting of an upcoming international legal guidance document on Contract Farming.

Ladies and Gentlemen, the Department of Agricultural Extension has the major role on promoting and developing occupation to uplift the quality of farmers' life. The Contract Farming system promoted by our Department is the one of model to assist farmers to meet with sustainability and security in their live. With considering demanding side, farmers has secure market and able to sell their products at reasonable price depending on quality, exporters get products with desired quality, quantity and delivery time, and processing plants get steady and good quality product supply.

I would like take this opportunity to share more detail on what you will derive from supporting Contract Farming. Contract Farming can solve the 3 major problems. These are agricultural marketing, farm management and farmer group organization.

Regarding to agricultural marketing, farmers have been quarantined product prices before growing and harvesting. They can sell their entire products with required quality under contract to buyers. This way will assist farmers to have a security on their career and certain income. Moreover, farmers have experienced increasingly on marketing demand.

Farm management is our expectation from promoting contract farming to farmers. Farmers will be well-trained for cultivation technique and farm management through farmer groups. Finally, farmers enable to plan in advance to maximize land, labour and input efficiently and worthily.

To develop themselves to meet the required criteria and have more power to negotiate product price with buyers, farmers will establish their group by themselves without forcing from outside. Not only the said benefits which farmers will gain from gathering the group but farmer group will also receive an advice and support from government through their group. This mechanism will appear prominently when farmer groups use their power to negotiate with buyers when the market price is higher against the quarantined price.

Distinguished guests and participants, please allow me to give you one example. Asparagus contract farming system project has been supported by our Department. The project initiated with Japanese Company in the western region in 1984. At the beginning, there were 580 growers, 6 groups with 240 hectare of production areas joined this project. In 2005, 4,457 growers, 62 groups, with 2,000 hectare of production area were interested to participate in the project. In addition, 10 exporting companies have been involved in the project and 60% of production areas are under contract farming system. This is the successful case from our Department's support which I would like to share to you all.

Ladies and Gentlemen, I wouldn't said that the Contract Farming has only the merit way. After we have extended the Contract Farming to farmers for over 20 years, we found the case which buyers refused to accept qualified products from farmers. In Thailand, the code on contract farming has no presented. In this case, the civil and commercial law had a crucial role to tackle with this problem.

However, the matter case like this has hardly occurred. Especially at present, our farmers have been familiar with buyers and some farmers' descendant has worked for buyer's companies in their area as well; therefore when the trouble situation happened, it was often ended by a compromise.

Ladies and Gentlemen, this workshop is organized by UNIDROIT in partnership with the Food and Agriculture Organization (FAO) and the International Fund for Agricultural Development (IFAD). As you know, these organizations are full of technical and academic skills. I am confident that you will fulfill your expectation from this workshop.

I will not lengthen speech further. We will soon be listening to all important speeches from Mr. Hiroyuki Konuma, FAO, representative from IFAD and Mr. Henry Gabriel from UNIDROIT. I hope that you will enjoy the deliberations. I also hope this workshop will be flourishing the workshop's aim.

Thank you all.

WELCOME ADDRESS

by Hiroyuki Konuma ¹

Mr Olan Pituck, Director General, Department of Agricultural Extension Ministry of Agriculture of Thailand,

Mr Benoit Thierry, Country Program Manager, International Fund for Agricultural Development,

Mr Henry D. Gabriel, Professor of Law, School of Law, Elon University (USA) and UNIDROIT Governing Council Member,

UNIDROIT, IFAD and FAO Colleagues, Ladies and Gentlemen,

Good Morning to you all,

It is my great pleasure to welcome you all to this FAO-UNIDROIT workshop on contract farming.

I wish to start by expressing my thanks to the organizers of this event, my colleagues from UNIDROIT, FAO and IFAD in Rome, for the invitation to greet you all here this morning and for selecting Thailand to host this important event. As some of you may know, Thailand hosts also the representation of FAO for the Asia and the Pacific Region, which I have the honor to lead.

The core theme of this event, contract farming, is high on the agenda of governments of most countries of the Asia and Pacific region, for a number of reasons I want to draw your attention to.

This region concentrates 70 percent of all smallholder farms of the world, or some 350 million of the 500 million smallholder farms that are estimated to exist today. The average area of these farms is about 1 ha. By and large, they face enormous challenges to have access to inputs, modern technologies, finance and markets.

In 2011, with about 4.2 billion people, our region also concentrated over 60 percent of the global population. Every year there are an additional 42 million mouths to be fed in Asia.

Asia is very rapidly urbanizing. While urban populations comprised only 18 percent in 1950, this had increased to 44 percent in 2010 and is expected to reach 56 percent by 2030. This is driven by the region's fast economic growth in many of the countries. According to the World Bank, the East Asia and Pacific region showed an average economic growth rate of 7.1 percent in 2013, while South Asia grew 5.2 percent. Economic growth in the region is leading to increased incomes.

Because of these trends, dietary habits are changing and so is the demand for intangible food attributes such as the ones associated with quality, diversity and supply regularity. Demand for non-grains and animal proteins is rising and so is the demand for processed foods and for food –away from home. Demand for certain grains, such as rice, instead, is declining on per capita basis.

Agriculture and food systems in Asia are being increasingly challenged to be more responsive to these changing consumer needs. Transformations are taking place primarily in the

¹ Assistant Director-General and FAO Regional Representative for Asia and the Pacific.

so-called “beyond the farm gate” activities that include logistics, wholesaling, processing and retailing

How do all these trends affect what are you going to be discussing here? Well, as FAO has been calling attention in some of our publications since a number of years now, the ways that food and agricultural systems have been traditionally coordinated need to change, so that open market systems more and more give way to closely aligned transactions between players in the agrifood supply chains, including the ones between the majority of smallholder farmers and the buyers of their products.

Contract farming is one of the mechanisms that can be help to improve efficiency and inclusiveness in transforming food and agriculture systems. In this region we have several examples of successful contract farming schemes for crops such as fruits and vegetables, and for poultry and forest products. In one of our projects, herbs and vegetables are being exported from Laos to Thailand for re-export to Europe and the Middle East. There are also examples of aquaculture in Vietnam, oil palm in Malaysia, hogs in China, and asparagus and Eucalyptus in Thailand. I am sure you will discuss more examples during your meeting of today.

Through these contracting schemes, buyers can ensure that they will have a regular supply of produce that meets quality requirements and are timely delivered. Farmers, on the other hand, can benefit from having a guaranteed market for their products and, in many cases, gain access to technology, inputs and financing.

FAO has been advocating responsible contract farming through our field projects and through our normative work. We maintain a web site that is specialized on this theme and we work with our member countries to build local capacity and raise awareness about contract farming. Each of the last two years we have conducted training courses for farmer-leaders, buying companies, and NGO and government facilitators on responsible contract farming.

A central consideration in our messages has always been the importance of an appropriate enabling environment for contracting to succeed in the agricultural sector. And it is self evident that a legal and regulatory framework that is conducive to contracting is a necessity.

The joint work of FAO with UNIDROIT and IFAD towards the development of a Legal Guide on Contract Farming, which will be the theme of your work today, is a very welcome initiative. It is also a very timely initiative for this region, where contact farming is being increasingly adopted, mostly because of the trends I summarized earlier on.

I suggest, however, that the outcome of the meeting should go beyond finalization of the document. I mean that important recommendations arising from this meeting should put forward for the consideration of policy makers as one of important outputs of the meeting.

I look forward to receiving the results of your work and I look forward very much to the final product of the collaboration with UNIDROIT, the Legal Guide.

Therefore let me wish you all a very productive day. For those of you who came from abroad I hope you have some time to enjoy Bangkok and perhaps to see more of this beautiful country.

Thank you.

WELCOME REMARKS

Benoit Thierry *

Excellencies,
Ladies and Gentlemen,
Dear Colleagues,

Welcome to this consultation workshop.

On behalf of the International Fund for Agricultural Development (IFAD), we are very happy to support this initiative. Contract farming may be a specialised topic, but it is now more and more important and a growing practice worldwide.

Before going deeper on this aspect, let me just remind you what IFAD is doing and who we are. IFAD is among the Rome-based agencies specialised in agriculture. So on the one hand, we are part of the United Nations system like the Food and Agriculture Organization and the World Food Programme, with a mandate for poverty alleviation in agriculture and this is very important; on the other hand, we are also an international finance institution – meaning, like the World Bank or the Asian Development Bank, we give loans to Governments to help Governments implement new policies to promote agriculture with smallholders. These loans are on quite concessionary terms. IFAD is working in almost 100 countries, so you can see our interest in contract farming because we have to work with small farmers. And how can we help the small farmers to get out of poverty, to make money, and therefore to link with markets? This is not very easy. Small-scale agriculture can be quite traditional; bringing people to market, which is a more modern way, is a bit complex so we can say that contract farming can be one interesting tool to implement that objective.

We have been trying many solutions you are familiar with and we look forward to hearing your experience and practice from your respective countries. But, you all know the progress that has been made in value chains and education in credit access. So, there are many solutions which can be implemented. But at the end the truth will be in the results, indeed how we are bringing products to the market, how we are bringing a new and better income to the farmers. Contract farming can be a key to bridge the gap between traditional agriculture and the market. I think there are many examples in the world on that. I used to work in Africa where these efforts are being developed. For instance, IFAD is involved in Uganda and Rwanda, in many important schemes with smallholders selling their products to bigger companies or bringing them to the cities. One example is oil palm. Oil palm may be grown not only on big farms but also on very small farms. It is also the case for tea and tea plantations, where people also can interact with a factory next to their door. But I would say that in Southeast Asia you know that very well. As Mr Konuma was saying, lot of smallholders in this region, and I think in countries like your country (Thailand), Mr Director General, has given the example that we can build really wealthy agriculture based on smallholders as long as these smallholders can produce the food, but can also produce excess and additional products to be sold on markets. Contract farming is quite developed here. So the same with China, with many smallholders, and with Vietnam, where success was built on smallholder agriculture and where there is quite a different model from other models as seen in America and Australia where you deal with very big farms.

* Country Program Manager for Cambodia, Philippines and Thailand - International Fund for Agricultural Development (IFAD).

So, one of my wishes is that Asia could inspire the rest of the world with a way of bringing small farmers into the markets and showing that you can have a successful agricultural sector thanks to smallholders. Here you have fifty years of experience showing that, in a modern economy, small farmers can succeed. So for IFAD it is very encouraging.

This is a very big exercise that we are engaged in with UNIDROIT and FAO and we are very happy to support it. Developing legal guidelines for contract farming is something which is quite complex and we are happy to see that it is progressing well. Why is it complex? Because contract farming is not new. It is a very old practice. We can even go back centuries if we want and many traditional ways of contracting currently exist in countries. I think the main challenge will be to make it modern, how to fit with the modern and legal framework.

What is important is, whatever the modern framework, that the farmers will have a certain level of education and practice. So I just want to say that we must be very careful to bring to farmers forms of contracts which can be perfectly managed by them and owned by them. I was happy to read in the many summaries and documents that there will be a focus on the fairness of the contract and we all know how it is important. Farmers, because of lower levels of education, can also be more vulnerable to companies who know the system better. So, how can we ensure that we have a win-win situation, as the FAO Director General mentioned? We need fairness, respect, and as we all know, any contract you make in the world starts with trust. So establishing this trust between the farmers and the contractors and the companies will be a very important step.

Another aspect that I see as quite complex is that cultures are very different in the world, even in Southeast Asia. So how can we adapt these contracting aspects to each culture in each country? There are ways to discuss and negotiate these contracts which may be different. And again, if we want the contract to be successful and respected by both parties, it has to also fit the culture and the practice in the country.

Contract farming can really be the next big thing in agriculture, for sure, but for that we need consultation and discussion and we are very happy that a small grant from IFAD can help this consultation process in America, in Africa, now in Asia and soon in Rome. The key objective we have to keep in mind is how can we go into contract farming for ensuring consumers better quality products, and offer the producers fair prices and sustainable practices. These are the two key elements which will make it a win-win situation.

So I wish you good discussions today. Do not hesitate to be practical, bring practical experience from your countries and then the lawyers of UNIDROIT will see how to fit that into the guidelines.

Thanks to UNIDROIT and FAO for this initiative and I am sure it will bring a lot for agricultural development and it will help all of us in promoting smallholder agriculture.

OPENING REMARKS

Henry Deeb Gabriel*

Distinguished speakers and guests,
Ladies and Gentlemen,

I would like to thank you for joining us at this consultation workshop “Promoting Good Contract Practices Between Producers and Buyers in Contract Farming Operations in the Asian Context” which is being jointly held by the International Institute for the Unification of Private Law (UNIDROIT), the United Nations Food and Agricultural Organization (FAO), and the International Fund for Agricultural Development (IFAD).

We have assembled an impressive group of experts to discuss practical experience, policy options and current problems of contract farming in the Asian Context. This workshop will help inform the drafting of the UNIDROIT/FAO Legal Guide on Contract Farming that will provide guidance and an internationally-recognised reference with a fair and balanced approach against which contract practices and public policies can be assessed.

The latest estimates by FAO predict that the world will have to nearly double food production within the next three decades to feed its population. To achieve that objective will require vast amount of resources, but also strong policies to channel investment towards agriculture and food production.

Growing population and higher standards of living have increased the demand for agricultural products, at the same time as consumer sensitivity to environmental issues and food quality lead to ever more sophisticated food markets. In this context, contract farming is expanding as a tool to organise and link production capabilities and market needs, to increase and diversify the availability of products on local and global markets, and to improve value chain efficiency.

As you know, vertical integration and supply chains are two of the main characteristics of today's agricultural markets. More than ever, they influence the way agricultural commodities are produced and how much is produced. Vertical integration and supply chains are structured around contracts linking the various actors, from the rural producer to the final consumer. A farmer's commitment to produce a certain commodity according to set specifications and production methods, is what is known as “contract farming”.

Contract farming offers many potential benefits, such as developing the production sector by contributing to capital formation, technology transfer, and increased agricultural production and yields. Consumers as well as all participants in the supply chain draw substantial benefits.

Governments are aware of the role that contract farming plays in agricultural development, and some governments have introduced policies, such as public private partnerships, to attract private sector investors and to coordinate ventures with local producers.

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Governing Council, UNIDROIT, Chairman of the UNIDROIT Working Group on Contract Farming.

Contract farming, does however, carry some risks such as over-dependency and other risks that typically affect the weaker party in a bargain.

The success of contract farming depends on many factors, but one key element is the ability of the parties to build stable, commercially sound and fair relationships based on clear commitments and mutual compliance. The contract is cornerstone of the relationship.

The law should make it possible for the parties to allocate risks, liabilities and economic returns fairly and efficiently. There should be predictable conditions for both performance and possible non-performance to ensure sustainable relationships and long-term financial benefits. These can be found either in the express provisions of the agreement or by mandatory or default terms otherwise provided by law. Regardless of the source, contract farming terms should reflect good practices and internationally accepted standards of transparency and fairness.

Can lawyers do anything to help make sustainable investment in agriculture more attractive? One may not think immediately of private law when thinking of food security. Yet the organisers of this workshop believe that an adequate legal framework for investment in agricultural production has a role to play in ensuring that sufficient capital is directed to the “real economy” of producing enough food to feed the world.

The food and agriculture organisations of the United Nations believe that, when properly structured, contract farming may offer farmers the opportunity of a secure revenue stream through guaranteed market access, higher yields and better quality from technical assistance. These, among other potential benefits, explain the interest of many national policy makers and international organisations in promoting sustainable contract farming models as a means for increasing agricultural production and improving the livelihood of the rural poor, thus helping to achieve food security worldwide.

FAO, for instance, implements national or regional development programmes, issues publications and runs a Contract-Farming Resource Centre. IFAD, in turn, support programmes that promote the inclusion of smallholder farmers in agricultural value chains and access to markets.

This is why both FAO and IFAD have joined efforts with the International Institute for the Unification of Private Law (UNIDROIT) to develop a legal guide on contract farming. The purpose of this work is to identify problem areas and possible solutions in light of current trade usages and legislation. The guide should serve as a “good practice” reference by providing advice to parties engaged in contract farming operations during the negotiation and drafting of contracts. The guide can also provide information for legislators and policy makers dealing with contract farming, in particular in the context of law reform.

UNIDROIT brings to this project nearly 80 years of expertise in developing international standards to unify and harmonise private law among nations, and is therefore well placed to coordinate this guide.

It is hoped that the guide will represent an additional tool for policy advocacy and capacity building which international organisations and bilateral cooperation agencies as well as nongovernmental organisations may use in their strategies and programs to support contract farming.

The working group set up by UNIDROIT to prepare legal guidance on contract farming, which is comprised of scholars, practitioners, international organisations, farmers and agribusiness representatives has held three sessions since January 2013 and is expected to substantially conclude its work later this year.

We have scheduled four consultation workshops this year throughout the world, in South American, Europe, Africa and here in Asia, to gather information about regional practices in contract farming.

The purpose of this workshop is to seek input from our Asian colleagues to ensure that the legal guide adequately addresses the needs and concerns of farmers in this region as well as the rest of the world.

I very much look forward to the discussions today. I believe they will provide valuable information on actual practices and needs of farmers that is crucial to help sharpen the advice we will provide in the guide.

I thank you again for having joined the workshop and wish you fruitful and interesting discussions.

Carlos Arthur B. da Silva, Ph.D.
Rural Infrastructure and Agro-industries Division
FAO – Rome




Contract Farming and Inclusive Value Chain Development



Contents

- Smallholders in global agriculture
- Challenges to link to smallholders to modernizing chains
- The renewed interest in CF and FAO's response
- What have we learned
- Conclusions







Smallholder agriculture is predominant: essential for livelihoods

Region/Country	Average Farm size (ha)	Smallholders (10 ⁶)
Africa	1.6	33
Asia	1.6	351
Latin America & Caribbean	67.0	5
Europe*	27.0	32
North America	121.0	—
China	0.4	193
India	1.4	93
Ethiopia	1.0	9
Indonesia	0.9	17
D.R. Congo	0.5	4
World	—	> 500


*Data include Eastern Europe for farm size only
 *Source: von Braun (2005), FAO World of Agriculture, Nagayets (2005), Altieri (2009), FAO (2014).

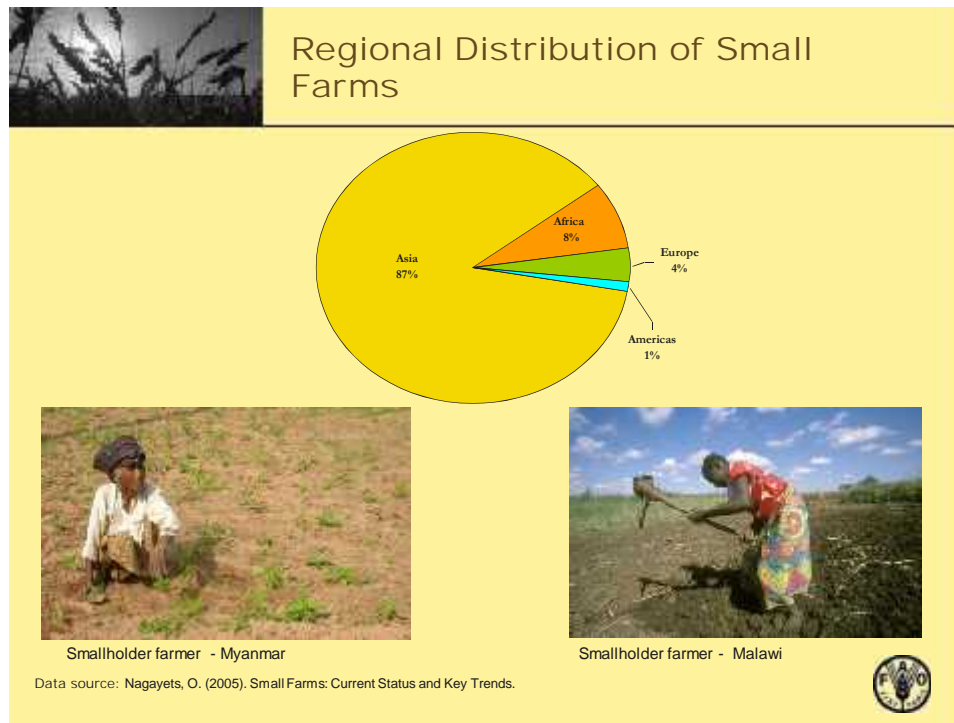



Small farms predominate worldwide:
 About 85% have less than 2 Ha;
 95% have less than 5 Ha

Region / Country	Farms with less than 2 Ha	(%)
ASIA		
China	189,394,000	98
India	92,822,000	80
Indonesia	17,268,123	88
AFRICA		
Ethiopia	9,374,455	87
Nigeria	6,252,235	74
D. R. Congo	4,351,000	97
AMERICAS		
Mexico	2,174,931	49
Peru	1,004,668	58
Brazil	983,330	21
EUROPE		
Russia*	16,000,000	98
Ukraine	6,214,800	99
Romania	2,279,297	58

* Less than 1 ha.
 Source: Nagayets, O. (2005). Small Farms: Current Status and Key Trends.





Challenges for the inclusion of smallholders in modern value chains

- High geographical dispersion; high assembly costs
- Are many and not well organized
- Tend to market small volumes
- Deal with dysfunctional input markets (lack of certified seeds, fertilizers, etc.)
- Lack services: credit, information, technical assistance
- How to address these issues?



What have we learned about linking farmers to markets?

- Main approaches to link farmers to markets
 - ◆ Producer driven
 - cooperatives
 - lead farmers
 - organized farmer groups
 - ◆ Third party driven
 - NGO's
 - Governments
 - ◆ Buyer driven
 - specialized wholesalers
 - traditional traders
 - **Contract farming**





Contract farming: concepts & definition

What

- ◆ *“agricultural production carried out according to an agreement between farmers and a buyer, which places conditions on the production and marketing of a farm product or products”*

Who

- ◆ Farmers
- ◆ Processors
- ◆ Traders, retailers / wholesalers
- ◆ Exporters

How

- ◆ Formal and informal agreements
 - Market specifications
 - Resource provision (inputs, finance)
 - Production management (technical assistance)





Why the renewed interest?

- Contracts are not a new concept
- Agri-food systems are being reshaped in response to global trends
- Supply chains need better coordination to promote efficiency
 - ◆ lower costs by improving productivity
 - ◆ improve and ensure quality throughout the chain
 - ◆ control risks associated with markets and food safety
 - ◆ enhance responsiveness to demand
- Interest in inclusiveness and social responsibility
 - **Contract farming as a workable mechanism to govern transactions in modernizing supply chains**
 - **A pathway for greater inclusiveness**



What is FAO doing in response to CF demand?

Dissemination of contract farming information

- ◆ Managing the *Contract Farming Resource Centre*

CF advocacy and promotion

- ◆ Expert roundtable on CF in Africa (2009)
- ◆ Frequent presentations of FAO experts in international events
- ◆ Articles, interviews, op eds. (e.g. article in WFO newsletter in 2013)

Capacity building

- ◆ Training workshops and planning and implementing responsible contract farming operations

Direct support to countries on regulatory frameworks

- ◆ Honduras, Nicaragua, El Salvador, Malawi, Morocco





What is FAO doing in response to CF demand?

CF Publications

- ◆ Contract Farming: Partnerships for Growth (2001)
- ◆ The Growing Role of Contract Farming in Agrifood Systems Development (2005)
- ◆ Overview of CF Legal Issues and Challenges (2012)
- ◆ Guiding Principles for Responsible CF Operations (2012)
- ◆ Special issue of “Food Chain”(2013)
- ◆ **New publication: “CF for Inclusive Market Access” (2014)**
- ◆ Training Manual on CF Planning and Implementation (forthcoming, 2015)
- ◆ UNIDROIT/FAO Legal Guide on CF (forthcoming, 2015)




CF and inclusive VCD




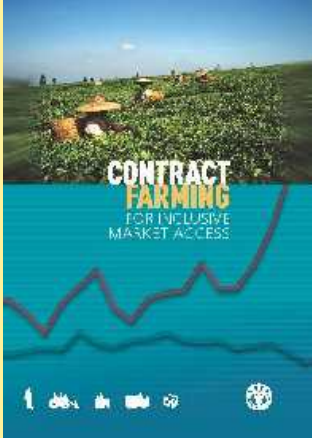
- **Can contract procurement be an effective institutional mechanism to enhance prospects for participation of small farmers in modern market channels?**
- **Case studies based on real world CF examples from developing regions**





The cases

- Poultry in Bangladesh
- Pork in China
- Citrus in South Africa
- Vegetables in Tanzania
- Cocoa in Honduras
- Grains in Argentina
- Basmati rice in India
- Biodiesel stock in Brazil
- Eucalyptus in Thailand



What are we finding?

- Expansion of CF will not necessarily lead to exclusion of smallholders from agrifood supply chains
 - ◆ Factors other than farm size play a role in the selection of suppliers (location, type of agricultural product, access to land, government incentives)
- Convergence in clauses & conditions, despite commodity differences
 - ◆ Market based pricing mechanisms, explicit quality requirements and penalties, penalties for non-compliance
 - ◆ Good contractual design important for inclusion





What are we finding?


- Provision of technical assistance and pre-financing of inputs: essential requirement for inclusive market access
 - ◆ Technology uptake essential to ensure ability to comply with quality; input pre financing also favors cost competitiveness
- Newer roles for third parties in CF operations
 - ◆ In addition to matchmaking, extension, financial intermediation and dispute resolution: third-party certification; commission agents providing value adding services; management certification



What are we finding?

- Side-selling inevitable, but:
 - ◆ Does not necessarily impede successful implementation & sustainability of CF with smallholders
- Government incentives can promote inclusion, but:
 - ◆ May pose risks to the CF scheme in cases of policy changes
 - Need for risk assessment in CF business plans






Challenges for CF success

Not a panacea


- Should be a good business proposition for all engaged
 - ◆ only sustainable if both partners perceive they are better off
 - ◆ mutual trust and reciprocal dependency
- An enabling environment (EE) is important
 - ◆ institutional and political setting must be conducive to promote long-term sustainability
 - ◆ legal framework must be in place
- Appropriate consideration of production, marketing and people-related risks in the CF planning strategy
 - ◆ Inclusion is not cost free!!!



Challenges for CF success

<ul style="list-style-type: none">■ Minimize potential for contractual hold-ups (farmer & firm)■ Countervail uneven balance of power<ul style="list-style-type: none">◆ promote group action◆ third party mediation◆ legal provisions■ Ensure gender equality■ Take into consideration environmental concerns	<ul style="list-style-type: none">■ Reduce transaction costs of dealing with multiple contracting parties■ Choice of enterprise<ul style="list-style-type: none">◆ no a priori exception◆ yet high value, processing and exports firms better candidates
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Legal Guide on Contract Farming (UNIDROIT, FAO, IFAD)

Guide to help address enabling environment issues

- Define CF from a legal stand point (typify CF contracts)
- Identify essential elements of CF contracts
- Promote good contractual practices for CF
- Present options for Governments to support /enhance/ regulate CF

Caveats

- Avoid over-protection of farmers/excessive regulation of firms
 - ♦ Can act as a disincentive for companies to participate in CF
- Potential for negative impact on farmers' access to finance, technical advice and markets
- Guide should promote trust building rather than confrontation



Conclusions

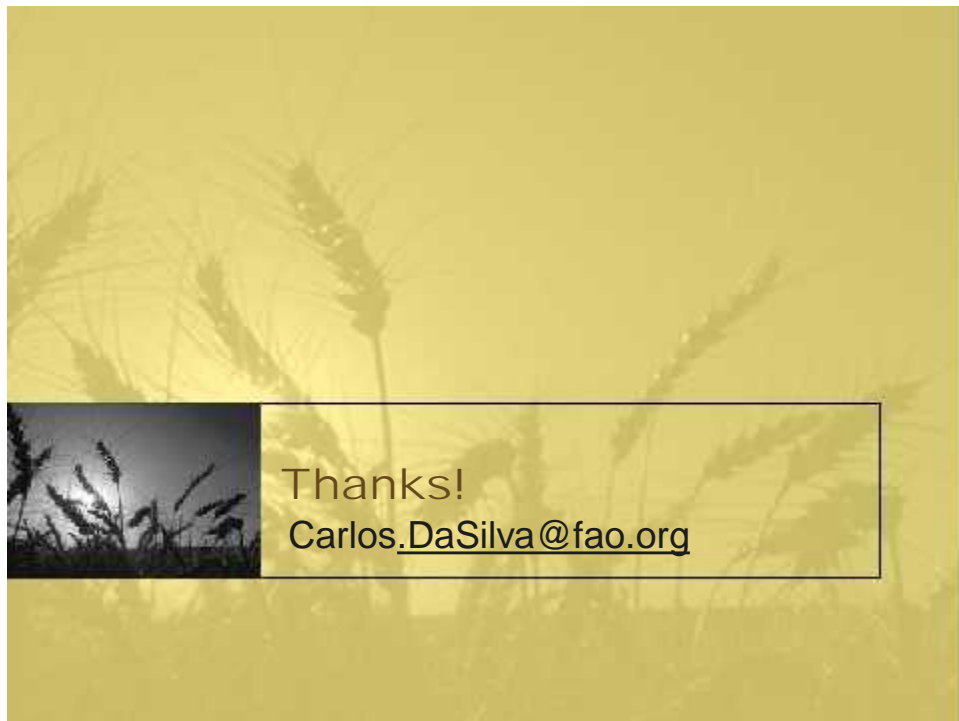
- As agri-food systems change, supply chains will become increasingly coordinated
- Smallholders will face increasing challenges to access chains
- Contracts are an appealing mode of governance and inclusion
- CF not a panacea
- Good planning and sound implementation essential to address production, marketing and people-related risks
- Appropriate legal framework is necessary
- Need for measures to maximize development impact





For more information

www.fao.org/ag/ags/contract-farming



Thanks!
Carlos.DaSilva@fao.org



Example: Pigs in China

- **Slaughterhouses targeting middle-class and premium markets**
 - ◆ Increasingly stringent quality and safety requirements
 - ◆ Need to source better quality pigs
 - ◆ Rapid switch from spot markets to contracting
- **Inspections**
 - ◆ Feed quality, disease control and medicines used, production hygiene and facilities, animal welfare
- **Services**
 - ◆ Feed supply, transport, extension training, veterinary support – not all processors offer
 - ◆ Information on prices, quality standards



Example: Barley in Argentina

- **Malt-beer value chain**
 - ◆ Market for malt barley highly concentrated
 - ◆ Asset specificity to meet manufacturer requirements
- **Specifications**
 - ◆ Type of seed, quantity and type fertilizer, weed control strategies, timing of harvest
 - ◆ Price based on wheat as reference (substitute crop)
 - ◆ Discounts / premiums according to protocols
- **Services**
 - ◆ Seed, agronomic advice
 - ◆ Some cases: co-finance fertilizer and agro-chemical inputs – but require farmer to buy insurance



CONTRACT FARMING: A LEGAL APPROACH

THE FORTHCOMING UNIDROIT/FAO LEGAL GUIDE TO CONTRACT FARMING

Professor Henry Deeb Gabriel ¹

You have in front of you an abstract that provides the structure and a blueprint to the Legal Guide on Contract Farming.² I would like to use the time I have this morning to give you the background of the Guide and why it is needed. I would also like to give some indication of the scope of the issues that we have attempted to address to give balance in the relationship between the parties.

Contract farming must be viewed as an important part of the overall development of food security and the development of agricultural production. Other elements of agricultural development, such as land tenure, equipment and inputs finance, as well as infrastructure for warehousing, processing, and transportation, also all play important roles. Among these varied aspects of the development of agricultural production, the current work of UNIDROIT has focused on contract farming.

Contract farming is agricultural production carried out according to an agreement between a contractor [buyer] and a producer [farmer], which establishes conditions for the production and marketing of a farm product or products. Typically, the producer agrees to provide agreed quantities of a specific agricultural product that conform to quality standards supplied by the contractor. In turn, the contractor commits to purchase the product and, in some cases, to support production through the supply of farm inputs, land preparation, and the provision of technical advice.

Contract farming arrangements reflect multiple commercial practices and their success depends on many elements. A key element is the capacity of the parties to build stable, commercially sound and fair relationships, based on clear commitments and mutual compliance. A reliable legal framework is essential to give legal effect to the parties' agreements and to supplement them as needed with mandatory or default rules.

In response to this recognized need, the UNIDROIT Governing Council, in 2012, agreed that UNIDROIT could usefully contribute its contract law expertise to the development of contract farming by preparing a legal guide on contract farming operations.

Thus far, there have been three meetings of the working group, and a last meeting scheduled in November. With luck, the draft will be presented to the Governing Council in May. As part of the project, in an attempt to be as inclusive as possible, we have scheduled four consultation workshops this year throughout the world, in South America, Europe, Africa and here in Asia, to gather information about regional practices in contract farming.

As you can see from the Abstract, the Guide focuses on the major legal issues in the contractual relationship between producers and contractors as well as other parties in the distribution chain.

¹ Chairman of the UNIDROIT Working Group on Contract Farming; UNIDROIT Governing Council member.

² Appendix A.

The structure of the Guide is set out like a commercial code. It begins with contract formation, proceeds with party obligations and responsibilities and ends with remedies. It is structured this way because contract farming is just a subset of commercial law.

What we have attempted to capture in the work thus far are the general principles that govern the agricultural production contract relationship within the very diverse legal world in which contract farming operates.

The contracts themselves may vary significantly in formality. Thus, while some contract farming ventures have detailed written contracts which are registered and monitored by the contractor; others may rely entirely on informal oral arrangements.³

The Guide is designed to provide general guidance on legal principles within the scope of best practices without targeting any specific domestic legal system. Contract farming is governed by a widely diverse set of laws. Given the global nature of contract farming, the Guide has to recognize both the common law as well as the Civil Law. In addition, part of the governing law could be international law. For example, to the extent that the core transaction is an international sale of goods agreement, the agreement might well be governed by the United Nations Convention on Contracts for the International Sale of Goods (CISG).

Within domestic legislation, contract farming may be governed by a variety of civil codes,⁴ agrarian codes,⁵ general contract legislation,⁶ specific agricultural contract legislation,⁷ and sector or product-specific legislation.⁸

³ In India, for example, companies contracting with hundreds of farmers for tomatoes and potatoes sometimes operate only on one-time oral arrangements with farmers.

In Indonesia, tobacco ventures often rely on oral agreements with tens of thousands of separate farmers.

⁴ For those countries with a civil code, in contract farming much of the general contract principles, such as formation will be governed by the code. The civil codes also generally provide default rules for how price is determined, general obligations of the buyer and seller, and a remedial structure. Regardless of other applicable law, the civil code will normally serve as overall background rules for the contractual arrangement.

⁵ Some countries have specific agrarian codes that regulate contract farming. This is the case, for example, in France, Panama and the United States (both federal law as well as many state laws). This often includes not only statutory frameworks, but detailed regulatory structures as well. Regulations often include the elements that certain agricultural contracts should indicate, including specification of the product, mutual obligations of the parties, contract duration and conditions for its renewal. The regulations and statutes often also cover force majeure clauses, arbitration procedures and provisions on compensation for damages in case of non-performance. The agrarian codes, such as those in the United States, Panama and France, are not comprehensive, and therefore much of the operative law will be governed by general contract law principles in civil codes or statutes that govern general contract law and case law.

⁶ Many countries have either general legislation regulating all contracts or legislation that regulates specific types of contract that would include contract farming.

⁷ Several countries have enacted legislation that specifically governs contract farming.

Spain is an example. Enacted in 2000, the legislation defines the principles that regulate contractual relations between agricultural producers, buyers and processors. The law provides sample contracts that are agreed upon among representatives of producers, buyers and processors and the Ministry of Agriculture, Food and Environment. The law requires that the contracts contain minimum standard clauses, and the contracts must be submitted for the competent authority's approval.

The law also establishes a monitoring committee which plays an important role in approving and promoting the use of sample contracts.

Moreover, in addition to the express terms between the parties, the underlying legal system may provide default and mandatory terms under both general contract law and specialized legislation that governs contract farming. Also significant, and captured in the Guide, is the importance of various industry and trade standards and codes. Within this wide array of potential legal frameworks, we have attempted to extract the best legal principles to suggest a means to create a fair and balanced relationship between the contracting parties.

Contract farming is typically established between producers and contractors. The Guide is intended to reflect the relationships and obligations among all of the parties throughout the supply chain from production to consumer, but the Guide is primarily directed to producers and the contractors of producers.

The producers may be individuals or they may be cooperatives or associations, which by forming groups and collectives, are able to increase their bargaining power. The contractor may run the entire gamut of entities from an individual entrepreneur to an international agribusiness company, a retailer or a wholesaler.

Broadly, contract farming can be either a sales or a service contract.⁹

Producers may agree to produce and sell to the contractor a specific crop or livestock with the contractor paying according to an agreed price determination. This is generally a sales contract.

On the other hand, producers may agree to provide a service for agricultural or livestock production that is owned by the contractor. This is a generally a service contract.

Producers may agree to plant and grow on their land the seeds provided by the buyer. This is a generally a service contract.

The Guide covers both sales and service contracts.

These different types of contract have different implications for the rights and obligations of the producers and the contractors, and the Guide has tried to capture this in an extensive chapter on party obligations.

The Guide specifically addresses the key provisions of an agricultural production contract and places them within the context of the parties' respective obligations. These include:

⁸ Several states in the US have product-specific legislation on contract farming, usually for the poultry and livestock industry. Another example is Kenya's Dairy Industry Act, which regulates the entire dairy industry, including contracts between producers and processing and trading businesses. The Act provides an oversight board, and requires the registration and licensing of dairy producers. Kenya has similar acts to govern sugar marketing.

⁹ A true employment contract is not contract farming, and what constitutes an employment contract from a contract farming arrangement may differ among such factors as whether the underlying legal obligation is Civil law or Common Law. Overview of Common Law perspective: The more control a company exercises over a worker's performance, the more likely the worker is an employee rather than an independent contractor. Provision of training, knowledge sharing by the buyer, and the continuity of the relationship between the buyer and the farmer are other factors that may indicate a possible employment relationship. Overview of Civil Law Perspective: Subordination is the factor that characterizes the employer-employee relationship. The employer is the party that gives directives to the worker, while the independent contractor is free to decide how to perform its duties and, for this reason, bears the risk.

The agricultural commodity that producers commit to sell or the service for agricultural production that they will provide.

- Inputs
- Contract duration
- Terms of payment
- Quantity and quality requirements
- Liability for inputs supply
- Risk of losses
- Product delivery
- Contract termination, and
- Dispute resolution

The Guide also addresses the major impediments to contract fulfillment, such as force majeure,¹⁰ market price fluctuations,¹¹ and change of government policies. The major risk in an agricultural production contract, though, is non-performance by one of the parties- a breach of contract; and this is one area that the Guide gives extensive treatment.

One source of potential breach is an inadequate understanding of the respective obligations. To help ameliorate this potential problem, the Guide gives extensive treatment of problem contract terms and clear guidance to avoid them. These include:

- Lack of clarity in price determination¹²
- Liability for production losses¹³
- Large investments required for a short-duration contract¹⁴

¹⁰ Force majeure refers to unpredictable situations that are beyond the parties' control, such as natural disasters or pest outbreaks. Agricultural production is particularly vulnerable to weather and disease. Extreme rainfall or drought, abnormally high or low temperatures, and pests or diseases could all devastate a farmer's production.

¹¹ Extreme market price fluctuations might make contract performance highly impractical. To protect the parties in this situation, contracts could provide for price renegotiation if the market price rises or falls outside specified limits.

¹² Clauses related to the determination of price are often unclear, complex or ambiguous, which can lead farmers to misrepresent or misunderstand how the price is calculated. Farmers may not always understand complex technical language. This is frequent in livestock production contracts where payment may be based on a complex formula combining factors such as the weight gained relative to the feed consumed, mortality and injuries. In crop production contracts, the price is often determined at the time the contract is entered into. Premiums and discounts may be applied in relation to quality, but in some contracts, the quality requirements demanded by the buyer ("grade specifications") are often not clearly specified.

¹³ Some contracts specify that farmers do not have title to the crops or livestock. (Normally, these are considered service contracts). This arrangement has two major advantages for contractors. First, contractors are able to retain intellectual property rights in the crop's genetic material. Second, the contractor is better able to prevent the producers' creditors from claiming legal rights on the object of the contract. These service contracts will typically impose some or all of the risk of production losses on producers.

¹⁴ When a short-duration contract requires large upfront investments by a farmer, the farmer is exposed to significant investment risks. For example, production contracts for poultry or livestock often require the construction of facilities built to exact specifications.

Unilateral termination clauses¹⁵

Confidentiality clauses¹⁶

Liability for environmental damage¹⁷

Abuse of mandatory arbitration clauses¹⁸

Throughout the Guide best business practices are emphasized. Although no legal guide can prevent unforeseen events or party misbehavior, the Guide directs parties to agreements that maximize incentives for efficient production and minimizes incentives to avoid party obligations.

Also emphasized throughout are the practical economic and business implications of a sound legal agreement. Thus, for example, the Guide encourages terms that provide for objective third party inspection of the goods to prevent one party from taking advantage of the counter party.

Likewise, parties are encouraged, where appropriate, to include provisions for contractor participation in production, technical assistance and close control over the producer's performance to enhance the quality of the final production to the benefit of both parties.

In this respect, the Guide goes beyond the strictly legal aspects of the relationship and provides guidance on the business aspects of the relationship. The goal is to provide a framework for long term sustainable business relationships that maximize the benefits to both parties.

Although the Guide focuses on the contractual relationship between contractors and producers, other parties, particularly those in the supply chain up to the consumer are affected by the agricultural production agreement. The Guide fully discusses these interests as they affect the primary relationship between the producer and the contractor.

The Guide is addressed broadly to three groups:

Parties involved in contract farming

Governments that want a guide for future legislation and policy formation for contract farming; and

The payback period for this capital investment may be long, so farmers could fall into serious indebtedness should contracts be cancelled or not renewed.

¹⁵ Some contracts include a unilateral termination clause, which allows buyers to terminate the contract at any time and for any reason.

In the case of large up front investments, unilateral termination clause poses great risks for farmers.

Other contracts allow buyers to terminate the contract in case of failure by the farmer to comply with the terms of the contract, without providing the complementary right to farmers.

¹⁶ Confidentiality or nondisclosure clauses may potentially create problems resulting from information asymmetry between contracting parties. A confidentiality clause prevents farmers from disclosing contract terms and conditions to other individuals. Thus, the clause may keep farmers from seeking outside technical and legal advice on contracts or simply comparing their contracts with those of other farmers to make sure they are getting a comparable and fair deal.

¹⁷ Because contract farmers are independent contractors, the risk of liability for the environmental damage that may arise from the production may be upon the producer.

¹⁸ In many contracts, producers are forced to sign mandatory arbitration clauses. This effectively forecloses recourse to the court system. Arbitration can provide quicker and cheaper dispute resolution but it is also important that farmers are informed and accept to use arbitration. Furthermore, arbitral tribunals might be more limited than a court for the types of claim that may be heard and the type of compensation that may be given.

NGO's that may be involved in the development and implementation of contract farming.

In summation, what have we set out to achieve with the Guide is an internationally-recognized reference on contract farming that provides a fair and balanced approach against which contract practices and public policies can be assessed.

I thank you for your time.

CONTRACT FARMING

Lawan Thanadsillapakul *

Introduction

Currently, patterns of agricultural production are changing. It has become more complex as the production of agricultural products through cooperation between farmers and entrepreneurs in agribusiness, so called "contract farming" will benefit the farmers to get products to the fullest. Volumes and value, as well as prices, increase. Farmers and agribusiness entrepreneurs would like to revolutionize and modernize traditional agricultural production to meet the increasing food needs of the population. It also supports social dynamics of agribusiness in the world.

The system of agricultural production through contract farming has been widely used in many countries around the world. This is because the system is beneficial to both farmers and agribusiness operators directly, affecting the economy in the state, such as helping to reduce risks for farmers. Farmers will earn steadily more. Contract farming reduces the risks and costs of agriculture and improves the quality of the products. Volume and the required number of products increase agricultural exports to foreign countries.

The definition of Contract Farming

The farming system under "contract farming" may not be as familiar as the basis of the more common general agriculture. Actually contract farming has been practiced in Thailand for more than 30 years, using different names, such as contract farming market deals or agriculture's chains. Having considered the meaning of the Covenant of Agriculture, the definition of agricultural agreement or contract farming could be as follows:

Baumann defines contract farming as a system of agricultural enterprises or agribusiness contracts to purchase agricultural products from farmers, with terms that may be different from some general agreement, but usually specify the amount to purchase agricultural products from farmers and agricultural price insurance to be purchased in advance from farmers. In general, the supply of credit to households and agricultural businesses, inputs, as well as providing technical advice in agricultural production to farmers are included. Essentially, covenants and the agricultural system under contract farming are a way to spread risk between farmers, producers and agribusiness operators. Endeavoring to agree on the terms of agricultural deals and to define a covenant from the beginning are the specific natures of contract farming.

Farming under the contract farming system is managing the relationships between farmers, manufacturers and buyers of products horizontally and vertically. The buyer can determine the course of the materials and agricultural products that they will buy. The buyers do not need to own a unit of agricultural plantation, also the farmers have the independence in agricultural production and own their own production units. The form of the contract is an agreement entered into between enterprises, agribusiness men and farmers prior to the production of agricultural products which will be based on the quantity and quality of agricultural production so agreed in order to supply the plant. (In the initial agricultural covenant is often the production of agricultural products for shipment to the processing plant) provided two important aspects: Buyers are

* Professor of Law, Sukhothai Thammathirat Open University.

required to ensure the production of farmers in terms of financial support, technical assistance, etc. in order to ensure quality inputs and services to enhance agricultural production. Agricultural extension services will be beneficial to farmers. It is also useful to agricultural producers in terms that it can ensure the market yield on farmers as priced purchase. However, some commentators do not support contract farming because farmers may have little bargaining power, at least less than agribusiness enterprises.

The Department of Internal Trade defines different agricultural covenant that means "agreement," form of agriculture or "Marketing agreement" with the definition of agricultural marketing covenant or agreement. "The commodity pre-agreement between farmers, producers, and buyer or institutional buyers or a processing plant or agent for various types, that enter into the settlement agreement in writing and specify the conditions for the production and marketing of products such as source of the arable land quantity, price, place of delivery, quality, payment, technical advice, and indemnity on a breach of contract, etc. The details of the agreement will vary according to the type of product and the parties.

The Office of Agricultural Economics defines the meaning of the agriculture agreement as the contract on the farm or farms where the provision of the means to produce crops or livestock are included in the agreements between the two parties which are manufacturers, including cotton farming and other agricultural contracts. The buyer, which is usually a company or the processing plant will mainly stipulate pricing. Including the standards and quality of output that will be purchased under the agreement in many cases is related to the supply factors of production such as technology, consulting, in agricultural production. The manufacturer will ensure the standard of output, according to the agreement.

The Agricultural Exposition Department defines contract farming as the production of agricultural products that have been agreed in advance between the farmers, manufacturers and buyers. The terms such as standard yield, the price, and terms of the delivery time will vary depending on the parties and the type of product.

Heartwood substantively evolved the definition of contract farming, focusing on helping farmers to achieve higher yields by reducing the cost of production per acre, and providing advice on the production technology. Minimum pricing is the key to the contract based on market conditions. If the price will be lower than the minimum price the products would be bought immediately. The principle of marketing looks at a binding contract which will specify the minimum cost plus a reasonable profit without notifying the minimum price beforehand.

Callahan and the Development Sub Committee define the characteristics of agricultural covenant as promised/agreed on terms of price and production system.

The buyers can determine the course of the materials and the agricultural products that they will agree to purchase and need not own their own production units. Farmers participating in the production of agricultural products perform the quality of agricultural products as agreed in the contract.

FAO has defined contract farming as the agricultural covenant which is an agreement between farmers and buyers. The processing or farming has created stability for the production and marketing of agricultural products that are sold under the prior agreement with the specified quality, volume, and price guarantee.

In the preparation of the agreement, it will vary. The definition of contract farming will relate to the development of the agricultural products and the production system, quality and quantity of

agricultural production, and farmers need to agree on the price of agricultural products in advance. In addition, the parties may determine the details of the contract as well as the production period. The process of agricultural production, delivery of inputs, monitoring of criteria for determining the purchase prices of agricultural products. The breach of the covenant of the agricultural system obviously is the failure to perform the obligation in delivery of quality products. Therefore, the benefit of contract farming will be to both parties.

Background of contract farming

The pattern of Greek contract farming is not complicated. In the first stage, it was agreed between the parties of the inputs to the farmers. In some countries, contract farming systems are used as a tool to increase the income of the farmers and to increase the quantity and quality of agricultural products as well as to stabilize the export of agricultural products. Contract farming has been introduced in the United States poultry industry.

Baumann also has reviewed the agricultural system under contract farming which was formed after the collapse of a large scale farming in the colonies, (which was established by the colonial countries for the exploitation of resources in the colony). After the declaration of independence of the colonies, the large farms of the colonies collapsed, along with the support of the newly gained independence and international organizations such as the World Bank, etc., and also to achieve harmonization.

The agricultural system of the contract has been used widely in many countries, both developed and developing countries including Thailand, the first country in Southeast Asia. Agricultural covenants were widely used in B.E. 2530, starting with the introduction of contract farming to agriculture and the suffered sugar cane production resulting in the success of sugarcane production systems as well as business operators and farmers. The government is starting to see the benefits of agricultural production under the contract farming system, and in turn to encourage farmers to produce agricultural products by using covenants, such as the color-coordinated with the cooperation of farmers. Agribusiness entrepreneurs, finance providers, and the Ministry of Commerce have a clear policy of supporting contract farming to the farmers until the present.

The result of the support of trade, such as supporting infrastructure offered the chance to point out the benefits of agricultural farm committed to provide price, export, and income stabilization.

Agricultural contracts are widely used in the production of agricultural products. In particular, Thailand relies on the production of traditional agricultural products and contract farming helps boost the exports of Thailand. Supporting contract farming, in addition to supporting domestic manufacturers, the government has promised to expand their farming neighbors under the Bagan Declaration.

Strategic economic cooperation Irrawaddy - Chao Phraya - Mekong. (Ayeyawady-Chao Phraya-Mekong Economic Cooperation Strategy: ACMCS), which is a collaboration between Cambodia, Laos, Myanmar and Thailand. The project is a collaboration of both the agricultural and industrial sectors. The forms of cooperation will support the marketing of basic inputs. Procurement and information exchange, including the use of national resources through the production of agricultural products through the agreement. Most investors would go into contract farming in Thailand, Cambodia, Myanmar, and Laos, which will be used in the output.

However, in the early stages of the adoption of contract farming used in both parties who support and oppose the function of farming covenants. Those who support contract farming

because they think that contract farming is an instrument boosting export of agricultural products. The opposition party reflects that contract farming is a testament to the farmers at their disadvantage because of their lower levels bargaining power under capitalism makes the true benefits of contract farming to the capitalists and to bind the non-capitalist farmers to perform the obligation under the agreement.

Types of contract farming

Agriculture under the contract farming create the farming ways that the parties are buyers who are engaged in farming and agriculture, the manufacturer agreed to provide maximum benefit for both parties to engage in agriculture. The farmers under different environmental conditions and factors make a commitment to agriculture in each country and each region that has its own variety. That is to coordinate the international market. Interests of agribusiness entrepreneurs and farmers will depend on the environment. Farming patterns may have changed over time. The modified model will be according to market change. The variation of contract farming has 5 forms.

1) The Centralized contract farming (The centralized model)

A centralized form of agriculture is a big project. Management system links together the various stages of production, procurement and marketing, the distribution of production, quotas to farmers, many of which are under the same project. This may lead to both crop and animal production. The buyers are business enterprises. Agricultural support from both local and foreign aid funds are used in production of agricultural product by the farmers. The level of support by agricultural entrepreneurs is different depending on the agreement.

2) The nucleus contract farming (The nucleus estate model)

The problem of most farmers is the lack of knowledge and lack of inputs that are used in the production of agricultural products that have to be a high quality and high volume. The nucleus estate contract farming model attempts to address this. Agricultural production under the covenant in the large projects and also in a combination system is generally agreed in advance. But contract farming is a different type of agreement with integrated terms and conditions. This will perform a demonstration or trial as an example to farmers to produce agricultural products for farmers to learn before production will be started. In some countries, the agricultural model of the nucleus is testament to the resettlement and relocation of farmers as well.

3) The Multilateral contract farming (The multiparty model)

Agricultural model of multilateral agreement is a model of agricultural production under contract farming with several covenants and people involved in farming, including government agencies, agribusiness entrepreneurs including other private organization of cooperatives and farmers in some countries, such as Mexico, Kenya, and West Africa. In China, the State will enter a joint venture with the private sector to the agricultural covenants. Foreign companies affiliated with the village committee also participate in farming covenants. But be careful to make sure that the products are standard and fair compensation. Without good management, multi-party cooperation system may collapse. In addition, the partnership may extend to the credit provider for the agriculture covenant. One point to be aware of the privileged experience of farmers' organizations and cooperatives may be using contract farming will not be successful according to the contract.

4) *The unofficial contract farming (The informal model)*

This agricultural model is an informal agreement which is often used to produce agricultural products with a simple and not very complicated production process. The covenant is an agreement between farming households, small businesses and farmers to produce an agricultural product that is seasonal. The crop is usually planted without a cumbersome process with less sophisticated techniques and inputs. The success of the agricultural production under this contract farming model is an informal agreement, which is based on the availability of support services, which are most likely to come from the government. In addition, the state is trying to find funding to support farmers for using such as capital to support the better production of agriculture. The farmers have been supported by agribusiness entrepreneurs. Another problem arising is legal problem, in many countries; there is a delay and inefficiency in the applicability of contract farming. Therefore, to breach of contract is easy. Farmers lack bargaining power may also easily be exploited. So, if the state has enough information to be able to bring free and fair trade to the input supply of the farmers in order to plan production process to meet the demands of the global market will be helpful.

5) *The contract farming with intermediaries (The intermediary model)*

Agricultural contracts with intermediaries will be a focal point for the collection of agricultural products to large agribusiness enterprises. Seeking to hire an intermediary to obtain the return of the products to the farmers is essential, however, the collection of agricultural products through intermediaries, making agricultural operators will have to bear the risk of receiving a lower standard because the agribusiness operator cannot control and inspection of agricultural products directly.

Considerations to determine the terms and details of contract farming

Contract farming is a special agreement that no law specifically stipulate the nature of the contract. Terms of contract farming constituted an agreement between farmers and agribusiness operators that can be contracted orally or in writing, depending on the parties to such agreement. It is necessary to consider the impact of the enforcement of contract farming the rights and obligations of the parties according to the agreement which is very important. The form and terms of the contract will depend on various factors such as the knowledge of the parties, bargaining power of the parties, the quality of the product, and other details. All terms specified in the contract shall be effective and beneficial to all parties. The agreement must have the legal details, management in the production process, and other essential details.

The most important considerations in determining the terms of contract farming

1) *The legal framework*

Contract farming is framed by the legal framework that will be applicable to those contracts, which is different from country to country. The terms of the agreement entered into by the parties have to be covered in every aspect including the event of a breach of contract. The terms in the contract farming with regarding to the law will make the parties be aware of the rights and duties of each party explicitly setting in the agreement in many forms. It can be a written or oral agreement that the parties made in advance, which usually are the business enterprises and the agricultural farmers that are contracting in advance.

2) *How to determine the price of agricultural products*

Variations in contract farming often differ depending on several factors. In order to maximize the cost, so the details of the agreement have a direct impact on returns made to the contracting parties, therefore, to get a return on their own terms. Details of terms to be specified in the contract is very important to give the parties the benefit of the contract fully. Terms defined in the agreement will be according to the quality of agricultural production under the contract. This is because the operators of agricultural inputs support knowledge and technology to farmers in order to meet the quality and quantity requirements, so the agreed returns based on product quality as a basis for paying the price to the farmers. However, the price of agricultural commodities defined by the quality of the product determines the variability of prices under the price range of agricultural insurance in advance. In addition, the agreement also includes specific details of the process control procedures to be used exactly as specified in the contract. Include determining the agreement shall cover the land of the farmers. The land is an important part in the production of agricultural products in the farming system. Especially in long-term contracts are used in agricultural production; the land used in farming in the agricultural covenant may be of the farmers themselves. The land may be leased from the farmers or other parties, or operators of agricultural land, or even from the government agency that land can be supplied to the farmers.

3) *The form of the contract*

Variations in the contract farming may be made formally that specified the rights and duties of the parties expressly to be bound by the agreement. This often happens in contract farming entrepreneurs invested in the contract. Another form of the model is to implement a system of registration for the production of agricultural products of interest to the agricultural system of the contract farming. By virtue of its simplicity in the agreement's flexibility, it is easy to understand the contracts which typically are open to registered farmers immediately after harvest. Then allocate production quotas to farmers as potential to the agricultural productivity.

Another form that is applied to contract farming is oral contract farming, without an agreement in writing. It often leads to problems of interpretation of rights, duties and obligations of the parties under the contract. This will lead to a misunderstanding of the parties and the disputes arising between the parties are difficult to be solved.

4) *The specific details of the contract*

The details of the agreement are clear on the rights and duties of the parties. It is important to make the parties to be aware of their rights, responsibilities and benefits to each party, so the party should have been covered by the terms of the contract period including the quality and standards of production quotas in cultivation practices, as well as the terms regarding delivery of goods, the agreed price, methodology of payment, and the arrangements for insurance.

"Contract Period" depends on the nature of agricultural production. Some of the plants agreed in the planting period for the short duration. In some plants may have to be flexible in the production period, such as tea, coffee, sugar and cocoa.

"The standard and quality of products" will affect the import of goods sold to consumers. This includes the expansion of agricultural production under the contract farming in the future. It may lead to the rejection of the goods specified in the contract. For determining the quality by the size and weight of the product, the problem is that the standard of quality is not clear. In some cases, the buyers have to pay the price for corruption and exploitation of contract farming implementation on one hand; on the other hand, the farmers are disadvantages in the contract farming agreement.

The Pricing issues may bring the dispute between the parties, so finding the process to calculate the price is the one thing that the parties must state clearly in the contract and it should be a simple and fair terms.

"Production quotas" will determine the quantity of goods to be produced in each contract. The quotas might be too much or too little. If the quotas are too much they will result in the product oversupply. But if they are too little they will increase the production cost per unit and the return will be low. The contract farming may lead to the project failure; therefore, processing the various areas to be used for the allocation of quotas for agricultural quotas should be clearly specified in the contract is important. Under the production quotas system, setting production quotas for farmers, specifying performance of farmers, and providing information to the consumer is essential. This includes the situation under the contract and the type of crops to be produced as well as the quality of the production process in the right amounts. If agricultural production does not match the number specified in the agreement may lead to various problems such as produce more than the amount agreed in the contract. Farmers are required to bring products to sell on the open market, which usually the price will be lower than specified in the contract, agribusiness entrepreneurs have the power to negotiate the purchase of agricultural products, too, from what is stated in the contract. But sometimes the price in the open market would be at a higher price than agreed in the contract. Thus this often leads the agricultural products to be sold outside the agreement. The agribusiness entrepreneurs will not get the quantity of product as specified in the quota as well.

The production process of agricultural products has to be strictly observed in order to meet the quantity and quality of agricultural products as stated in the contract. Farmers have to apply inputs to agricultural production under the contract at the request of agribusiness enterprises. It will not be applied in contract farming unless otherwise stated in the agreement; the agreement must also restrict farmers' inputs such as chemicals prohibited by the law or caused a negative impact on the consumers or the farmer's actions may bring losses to agribusiness entrepreneurs. In addition, farming operators also need to understand the farmers' agricultural production process strictly, as well as to determine the production methodology.

"Preparation of shipping agricultural products," the process of preparing this must begin since the preparing stage for the harvest unto the export of agricultural products, the details of harvesting and shipping will vary depending on the terms of contract farming. To take delivery of goods has to be negotiated properly. The process of commodity shipping is very important to be taken into consideration. The employees of enterprises and agribusiness in the verification process the harvest as well as the transport processes are to be settled in the contract farming.

"Preparation pricing and payment "is the most important part of the contract because farmers will focus on the results to be derived from the production of agricultural products, so how to define in the pricing and payment process must be transparency. It is important to make a successful farming covenants and agreements together with sustainability. The method to determine the form of payment varies. The various formats include the followings.

1. The most common pricing is to specify a **guaranteed price** before the operation will start based on the quality of the agricultural products to be produced that determines the price. But this constant agribusiness entrepreneur will have to bear the risk of market price fluctuations. And farmers are likely to produce the goods in according to the contract farming, if the price of the agricultural goods specified in the contract is lower than the market; it may cause the market leak, the entrepreneurs have always set the terms for saving themselves in case of breaching the contract by the farmers. On the other hand, the farmers will benefit from the price and have

advantages over the agribusiness entrepreneurs in terms of costing and marketing as well if the agreed price is over the market price

2. **The price elasticity**, flexible pricing is determined based on the price of agricultural commodities in the world market or local market. Farmers are paid based on costs and prices in the world market. The price for transactions in some foreign countries such as the Philippines, agriculture and agri-business entrepreneurs will be rewarded equally. After deducting the cost of agribusiness enterprises, farmers will use this deduction as the inputs. The storage market value of the risk, if the price drops before delivery the flexible price is necessary for trust, mutual understanding, and mutual benefit between the farmers and the buyers. They must be very honest to each other.

3. The prices are calculated based on **market prices**, as a form of pricing is complex and it may lead to misunderstanding and error-prone, we need a common understanding about the model to determine the price based on the market price. But farmers need to produce higher quality products to market in exchange for guaranteed income.

4. "How to Pay", the most popular method to pay farmers to produce agricultural products is to pay cash. This usually is the most convenient payment options. However, the cash payment may not be made in some cases. The parties may agree to pay any relevant agricultural commodities after harvest or other suitable method as the parties shall agree.

5. Preparation of Insurance Farming investment using contract farming will be complementary to the contracting parties: farmers and agribusiness entrepreneurs. However, the investor may have risk factors that may make investments suffer losses such as natural disasters, disease outbreaks or may be caused by human actions, including the volatility of prices, etc. These risks can be managed to solve the problems. Losses insurance by agricultural commodities produced under the contract farming may be done. Despite the extra costs, it will help manage the risk to farmers and agricultural businesses. If an unexpected event occurs.

Advantages and disadvantages of contract farming

Currently, the global demand for food increases constantly. Therefore, new technologies are required to produce more agricultural products. Making the transition from traditional agricultural production to using modern technology and inputs will yield more and progressive results with both the quality and quantity sufficient to meet the needs of the global market. Modern agriculture relies on the transfer of the means of production and technological progress through the contract farming.

Contract farming has been used in agribusiness from the past to the present, to reduce costs and help spread the risk to the agribusiness enterprises. It also allows farmers to develop the skills and technology for agricultural production process and sustainability. With the support of contract farming systems in developing countries since 1990, the government has encouraged local farmers to benefit from contract farming from farm to farm gradually facilitating by the government's joint venture with a private company. Subsequently, contract farming between corporate farming to farmers applying agriculture covenant is used in the production of agricultural products. An important role of contract farming in the development of agricultural production process enhances income for farmers in those countries.

The Contract farming is an agreement between one or more people, farmers and business entrepreneurs dealing with the agricultural production process which has been agreed in advance on the quality, quantity, time of delivery, the price of agricultural products to be delivered in the

end of each agricultural product processing. Farm prices are guaranteed in advance. The contract may be either written or verbal. The contracting parties often have to renew the contract farming if there is mutual confidence. In determining the terms of the covenant typically must contain at least four distinct commodity terms: agricultural product quality, quantity, and time of delivery of agricultural products, and the price of the goods. There also may be specified in the contract, such as the duration of the contract, quality control, and packaging. Risk of delivery relates to the pricing mechanism, which may be a fixed or flexible price. How to pay insurance, as well as a method of dispute resolution are also have to be determined in the covenant of contract farming focusing on risk allocation especially the mechanisms for determining the price of agricultural products.

However, contract farming has both advantages and disadvantages to both farmers and the companies that are parties to the contract due to several factors such as the different interpretation of the terms of contract, price fluctuation, bargaining power, the insufficient knowledge of the farmers, unfair contract terms, ineffective management, chemical inputs that harms the soil, insufficient financial support, and many more factors that need help from the government and international institutes to formulate the fair terms of contract farming and the monitoring of good practice of both parties: the farmers and agribusiness entrepreneur.



Country Overview on The Legal Framework for Producer-Buyer Relationships in Philippines

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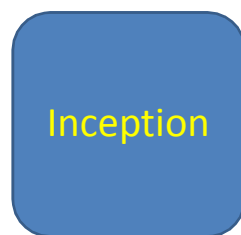


THE PHILIPPINE REGULATORY FRAMEWORK

Stages of Contract



1st Stage of Contract



- Juridical Entity Not Designed for Business

•CONTRACTING PARTY ISSUES

- Juridical entity assumed to be owner of the land or has control of the land (the fatal assumption)
- Composition and membership (AR beneficiaries or ordinary farmers???)
- In the Philippines, the default Cooperative or non-stock, non-profit Corporation
- Farmer friendly Registration and Compliance Requirements ????????
- Organizational Management is Challenging

Stages of Contract

Inception

•Bargaining Power

- Smallholders lack knowledge and skills in Negotiation of Commercial Contracts
- Smallholder have no value added products and services to leverage in the negotiation process

ROLE OF GOVERNMENT?

Stages of Contract

Inception

•Information Access

- No central repository of relevant and updated data for smallholders when they enter into Business Contracts
- Prices on inputs and produce are controlled by private Groups

•Credit Support

- Money is available, but financial Institutions are wary to lend due to the lack of information on the characteristics of the borrower ----- risk management

2nd Stage of Contract

Creation

- Form and consent requirements are sourced from the Civil Code of the Philippines and relevant laws
- During contract negotiation: who represents the smallholders?
 - Legal and business advise

Stages of Contract

•Review and Approval

Creation

- Government reviews contracts involving agrarian awarded lands
- the standards (essentially vague and unclear)
 - DOES NOT result in change of use to non-agricultural land
- General criteria:
 - Guarantees security of ownership and tenure
 - Increased income

Stages of Contract

•Review and Approval

Creation

➤contract terms:

- SUFFICIENT AND RELIABLE BASIS THAT AGREEMENT IS ECONOMICALLY VIABLE AND PROFITABLE
 - Realistic rates of return
- Period mutually agreed based on nature of activity
- Review based on extraneous events/subject to approval process
- Maintaining viability of juridical entity
- Workers' productivity
- Specific provisions to protect AR beneficiaries based on type of arrangement
- Safeguards to ensure risk management (insurance)
- LEASE – minimum amount must be more than land amortization and taxes + poverty threshold
- **Ecological soundness**
- **Skills development of AR beneficiary**
- **Non-transfer of land**

3rd Stage of Contract

•Monitoring of Contract Implementation

- The government requires regular submissions from the parties of audited financial statements and development progress of agribusiness contracts

Implementation/ Dispute Resolution

Government Capacity to Monitor Commercial Contracts Must be Developed

3rd Stage of Contract

•Jurisdiction

- Applicable law? agrarian law, civil law or commercial laws
- Arbitral Clauses in the Contract
- Private or Public resolution

Implementation/
Dispute
Resolution

Alternative Dispute Resolution assumes a fair contract

3rd Stage of Contract

•Grounds for Review

- After 5 years, welfare (?) of AR beneficiary has not improved
- Violation of contract
- HR development provisions not followed
- Non-employment of AR beneficiaries (retirement??)
- Fraud
- Concealment of financial status
- Financial and economic viability
 - Change in prices of input and output
 - Inflation rate
 - Disaster
 - Force majeure
- Land is devoted to other uses without consent of AR beneficiaries
- Transfer of land to investors
- OTHER meritorious grounds

Implementation/
Dispute
Resolution

3rd Stage of Contract

- DAR Adjudication Board (DARAB)
 - Quasi-judicial Body
 - Tenure issues over farmland
- Presidential Agrarian Reform Council (PARC)
 - Policy making body under the Executive Department
 - Approval and Revocation of Contracts involving agrarian awarded lands
- Regional Trial Courts
 - Judicial Bodies
 - Inter and Intra-organization disputes
 - Civil Code and Civil Law provisions

Implementation/
Dispute
Resolution



POLICY QUESTIONS



Policy Questions

1. Juridical Entities for Smallholder Farmers
 - Appropriate entity for smallholder farmers?
2. Curing the Information Asymmetry
 - Government's role ensuring availability of key information to smallholder farmers in contract farming.
3. Availability of Resources and Technology
 - Bargaining chips for the smallholder (pump prime)
 - Government's role in technology improvement and availability in contract farming.



Policy Questions

4. Dispute Resolution and Remedy
5. Food Security, Climate Change and Land Tenure
 - Government's role in ensuring social objectives of agriculture in contract farming arrangements.
6. Credit, Agricultural Technology and Business Development Services
 - Levelling the playing field
7. Agriculture as a pathway out of poverty
 - Making agriculture profitable
 - It isn't just agriculture



Standards for Review and Approval

- Voluntary Guidelines on Land Tenure (VGLT) and the Draft Principles of Responsible Agricultural Investment (PRAI) like:
 - Recognizing and respecting the control and ownership rights of smallholders farmers over their farmlands.
 - Provide access to legal remedies to deal with infringements of legitimate the smallholder farmers' tenure rights.
 - Provides Government mechanism to ensure that agricultural agreements will uplift the economic conditions of smallholder farmers and upgrade their technical knowhow.
- 



Adoption and Effective Implementation of the VGLT Principles will answer most of the questions

1. Human dignity
 2. Non-discrimination
 3. Equity and justice
 4. Gender equality
 5. Holistic and sustainable approach
 6. Consultation and participation
 7. Rule of law
 8. Transparency
 9. Accountability
 10. Continuous improvement
- 



UNIDROIT Guidelines on Contract Farming

- Clear documentation
- Readability of contracts
- Due attention and review
- Disclosure
- Transparency in price determination
- Transparency and fairness in clauses related to quality
- Transparency and fairness in clauses related to input supply and use
- Fairness in risk sharing: force majeure and contractual flexibility
- Prevention of unfair practices in buyer-farmer relations
- Honouring contractual terms
- Open dialogue
- Clear terms to settle disputes



Proposed PRAI Principles Gives Light to some Gaps

1. Existing rights to land and associated natural resources are recognized and respected.
2. Investments do not jeopardize food security.
3. Investment processes is transparent.
4. Consultation, and agreements are recorded and enforced.
5. Investors ensure that projects respect the rule of law, reflect industry best practice, are viable economically, and result in durable shared value.
6. Investments generate desirable social and distributional impacts and do not increase vulnerability.
7. Environmental impacts of a project are quantified and measures taken to encourage sustainable resource use.



Policy Questions

INCREASING BARGAINING POWER

Versus

REGULATION



APPLICABLE RULES

Republic Act 6657 (as amended)
Republic Act 8799 (2000)
DARAB Rules of Procedure of 2009
DAR Administrative Order No. 9, Series of 2006

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Protection for Smallholders in Oil Palm Industry in the Partnership Scheme in Indonesia

By

Paripurna P. Sugarda

I. Introduction

The oil palm industry has become one of the most important and strategic industries in Indonesia. With global production of palm oil in 2012 amounting to more than 50 million tons, Indonesia took the share of more than 50% or 28.5 million tons with annual growth of 6.7%.¹ From this amount of production, 47% or 20.6 million tons is to be exported.² The production of the oil palm industry is done by more than 50 big companies. They plant, cultivate, and process the oil palm using the service of, among others, smallholders, mostly surrounding the area of the productions, individually or through the establishment of cooperatives.

This paper concludes that Smallholders are in the weak bargaining position in almost every aspect in the oil palm partnership contract like capital, expertise, accessibility to production and market, and its position in the monopsony market structure. Government through its regulation tried to protect Smallholders, but the protection is given through the opportunity for them to enjoy the industry of oil palm in which companies, in order to get license of IUP, IUP-B and IUP-P have to involve Smallholders. The government does not give sufficient protection through the standard of Partnership Scheme Contract that has to be made by smallholders and a company.

The contract that is made by parties is in need to be improved. The main lack of the contract is the absence of complete provisions regarding in the “event of default” and force majeure.

To strengthen the bargaining position of smallholders, encouraging them to form cooperatives may increase their bargaining position in many aspects like fund, capital, technology, and market access.

II. Method of Analysis

This research uses a legal normative approach. This normative legal research is based on library research. Two contracts on the oil palm Partnership schemes are to be analyzed in this paper. A descriptive analytic research result is to be expected from this research.

¹ Oxfam Discussion Paper, 2014, Fair Company-Community Partnership, www.oxfam.org. p. 8.

² Loc.cit.

III. Regulations on Oil Palm in Indonesia

In order to provide a legal basis in the provision of services and the implementation of licensing of plantation businesses, in order to provide protection, empowerment for plantation business actors in fairness and certainty, the Indonesian government launched Regulation of Ministry of Agriculture of Republic Indonesia Number 98/Permentan/OT.140/9/2013 (Regulation of MoA No. 98/2013) regarding the Guidelines for Licensing of Plantation Businesses.

Based on the regulation, the maximum plantation area applicable for a plantation company or a Group of Plantation Companies for oil palm is 100,000 hectares, but state-owned companies, regional government-owned companies, cooperatives and publicly listed companies *in which the majority of shares are owned by the public* are exempted from this limitation.³ The regulation stipulates that a plantation company which is applying for an IUP-B (plantation business licence for cultivation) or IUP (cultivation and processing integrated plantation business licence) with a total plantation area of 250 hectares or more is obliged to 'facilitate' the development of community plantation for the surrounding community located outside the plantation area of that plantation company, with a total area of not less than 20% of the total plantation area under its IUP-B or IUP.⁴ This provision makes it clear that a community plantation development is to be calculated outside the total plantation area of the plantation company.⁵ The regulation also specifies that the 'facilitation' can be done by way of payment on credit, revenue sharing or other form of financing.⁶

According to Art. 9 of the regulation, Industrial Businesses of Oil Palm Processing with capacity achieving to 5 tons of TBS (Fresh Fruit Bunches) per hour at minimum in the form of CPO, palm kernel, fiber and sludge are obliged to hold IUP-P (processing plantation business license).⁷ In order to hold IUP-P mentioned in Art. 9, the Industrial Business of Oil Palm Processing must fulfill the need of raw material at a minimum 20% from its company, and the remaining needs of the raw material have to be fulfilled by the society plantation/Plantation Company that does not own the processing unit and has no partnership scheme relationship with any Industrial Business of Oil Palm Processing yet, through continuous processing partnership scheme⁸.

The partnership continuous processing scheme as referred to in Art. 11 shall ensure the availability of raw materials, the formation of a fair market price, and the realization increase in value added on an ongoing basis for the planters.⁹ The partnership scheme of continuous processing has to take the form of a writing and duly stamped agreement for a period of at least 10 (ten) years and subject to be reviewed on a minimum of every 2 years according to the agreement.^{10 11}

³ Art. 17 (2), Annex VI, and Art. 17 (3) of the Regulation of MoA No. 98/2013

⁴ Art. 15 (1) of the Regulation of MoA No. 98/2013

⁵ Art. 15 (2) of the Regulation of MoA No. 98/2013

⁶ Art. 16 (1) of the Regulation of MoA No. 98/2013

⁷ Art. 9 and Annex II.

⁸ Art. 11 of the Regulation of MoA No. 98/2013

⁹ Art. 12 (1) of the Regulation of MoA No. 98/2013

¹⁰ Art. 12 (2) of the Regulation of MoA No. 98/2013

¹¹ Art. 9 and Annex II.

In order for an oil palm processing company to obtain an IUP-P (plantation business for processing), it must secure at least 20% of the oil palm that it will process from its own plantation. Otherwise, it will need to (i) seek a statement from the relevant local authority in charge of the plantation to confirm that there is no vacant land left for it to be able to build a plantation (in order to supply 20% of the oil palm that it will process) and (ii) enter into an agreement with the cooperative of planters in the area. Please note that in entering into such an agreement with any such cooperative, the oil palm processing company will be further required to sell some of its shares to the cooperative, amounting to at least 5% in year five and 30% in year 15.

In addition to this community plantation obligation, a plantation company is also expected to enter into partnerships schemes with planters, employees and the surrounding community by assisting with supply of production facility, production support, processing and marketing support, transportation, operational services, *share ownership* and/or other supporting services.¹² The Partnership Scheme is based on the principle of mutual benefit and sustainable benefit, mutual respect, mutual responsibility, and strengthening each other.¹³

The regulation provides a standard of contract of partnership scheme to be followed, mentioned on the Annex II below (Art. 1, Section (1-4)):¹⁴

- “(1) The First Party (Company) has a duty: (a) to receive raw materials from the Second Party with volume, quality, frequency and time will be according to the agreement; (b) to make a payment to the Second Party in accordance with the price, volume, quality, and time agreed by the parties; (c) along with the regent / mayor gives cultivation techniques of construction, engineering and the timing of harvesting, introduction of quality, handling harvest, .. etc.
- (2) The First Party shall have the right: (a) to reject raw materials sent by the Second Party when incompatible with the standard, which was agreed. ; (b) to get good quality of raw materials agreed by the parties; c.
- (3) The Second Party has the obligation: (a) to provide raw materials to the First Party with volume, quality, frequency and time of delivery according to the agreement; (b) to make appropriate cultivation techniques comply with technical standard so as to generate good quality of raw materials; (c) to harvest in a timely manner and in accordance with the proper harvesting technique ; d.
- (4) The Second Party has the right: (a) to receive payment from the First Party with appropriate price, volume, quality and time agreed by the parties; (b) to seek guidance from the First Party for cultivation techniques, techniques and timing of harvesting, introduction of quality, harvest handling; c.”

IV. An Overview on Indonesian Contract Law

¹² Art. 29 and 31 of the Regulation of MoA No. 98/2013

¹³ Art. 30 (1) of the Regulation of MoA No. 98/2013

¹⁴ Annex II of the Regulation of MoA No. 98/2013

Indonesian contract law was formalised in the year of 1847, as laid down in Book III of the *Burgerlijk Wetboek voor Indonesië, Staatblad 1847:23* and until presently, it has never been amended notwithstanding the growth of transactions made in the business world which have become more complicated. This paper's intent is to evaluate only one of the most important things in contract that is breach of contract. In this regard, this paper is trying to compare Indonesian Contract Law and the New Dutch Contract Law considering that Indonesian contract law has actually originated from Dutch Contract Law.

A. Breach of Contract and Its Remedies: a comparison between Indonesian and Dutch Contract Law

Most Indonesian scholars use the term '*wanprestasi*', originated from Dutch term '*wanprestatie*' to describe non-excused non-performance. Satrio, for example, states that:¹⁵

"In case the debtor does not fulfill his obligation or does not fulfill his obligation as is supposed to be, and he does not fulfill his obligation because of the existence of a fault on him, there are several legal consequences – due to the creditor's claim – against him."

This statement is made under the heading of '*wanprestasi*' in general. In line with Satrio, Setiawan asserts that:¹⁶

"The debtor is obliged to fulfill his duty to perform. And if his non-duty is not because of force majeure, he will be considered as breaching his promise."

This statement is asserted under the heading breach of promise (*wanprestasi*). It is notable that some Indonesian scholars do not give any attention to the term excused non-performance under the heading of *wanprestasi*. Only after they come into the discussion under the heading of force majeure, they restate their first explanation: that only when there is a fault then someone can be adjudicated breach of the contract. Subekti, for example, states that:¹⁷

"If the debtor does not do what he has promised, he will consider being *wanprestasi*. He is negligent or breaches his promise. Or also, he will be considered in breach of contract if he does something that he, according to the contract, was not supposed to do."

¹⁵Satrio, J., *Hukum Perikatan, Perikatan Pada Umumnya*, Penerbit Alumni, Bandung, 1993, p. 144 [hereinafter Satrio, *Hukum Perikatan*]

¹⁶Setiawan, R., *Pokok-Pokok Hukum Perikatan*, Binacipta, Bandung, 1994, p. 17. [hereinafter Setiawan, *Pokok-Pokok Hukum Perikatan*]

¹⁷Subekti, *Hukum Perjanjian*, Penerbit PT Intermasa, 1987, Jakarta, p. 45 [hereinafter Subekti, *Hukum Perjanjian*]

Similarly to Subekti, Gautama explains that:¹⁸

“An obligor should perform his obligation at the time and in the manner agreed. If he fails to do what he has promised - either by not doing it at all, or by delaying it, or by doing it in a way contrary to the terms of the agreement - or he does something which is prohibited by the contract, he may be in default and become liable for damages or some other remedies available to the obligee.”

The statements made by those two scholars may mislead readers because they do not state the fault element when describing the term “breach of contract”. Putting the chapter or section of supervening events before the chapter or section of non-performance might help readers to keep in mind to always consider the existence of excused non performance, as many scholars do.¹⁹

Although generally the idea of (excused and non-excused) non-performance, breach of contract, and default as recognized in Indonesian Civil Code is similar with the Dutch Civil Code, the Indonesian Civil Code arguably sets out the principle in a more restricted manner. Article 6:74 and Article 6:75 of Dutch Civil Code distinguish excused and non-excused performance. Article 6:74 (1) of Dutch Civil Code states that:²⁰

“Every failure in the performance of an obligation obliges the debtor to repair the damage which the creditor suffers therefrom, unless the failure cannot be imputed to the debtor.”

Furthermore, Article 6:75 of Dutch Civil Code provides that:²¹

“A failure to perform cannot be imputed to the debtor if it does not result from the debtor’s fault, and if he cannot be held accountable for it by law, juridical act or common opinion either.”

The debtor’s failure to perform is excused if he can prove that it is not due to his fault and if he cannot be held liable for it by law, juridical act or common opinion either. Indonesian Civil Code also has the term breach of contract (as called *wanprestasi*), which shares the same meaning with the Dutch Civil Code, namely, the debtor does not perform his obligation and he cannot establish that this is not because of his fault. A fault cannot be attributed to the

¹⁸Gautama, Sudargo., *Indonesian Business Law*, Penerbit PT. Citra Aditya Bakti, Bandung, 1995, p. 88. [hereinafter Sudargo, Indonesian Business Law]

¹⁹See, Beale, *Ius Commune*, p. 592; Beale, H.G., Bishop, W.D., Furmston, M.P., *Contract Cases & Materials*, Fifth Edition, Oxford University Press, Oxford, p. 459; Smith, *Atiya’s Introduction*, p. 241, Wissink, *International Contract Law*, p. 95.

²⁰Translation by Haanappel P.P.C., Mackaay, Ejan, *Nieuw Nederlands Burgerlijk Wetboek, Het Vermogensrecht*, Kluwer Law and Taxation Publishers, Deventer, 1990. p. 260 [hereinafter Haanappel and Mackaay, *Nieuw BW Translation*].

²¹ Loc.cit

debtor if his performance is obstructed by unforeseen events or force majeure.²² This can be reflected from Article 1244 Indonesian Civil Code which stipulates that:²³

“If there is any reason for such a situation the debtor must be punished to compensate for the expenditures, losses, and interests, he cannot prove that the unfulfilling, or the unpunctual fulfilling of the agreement, was caused by unforeseen events, and thus could not be imputed on him. All of that are dependent on the condition that he has no bad faith.”

Also Article 1245 provides that:

“There are no expenditures, losses, and interests that shall be compensated, if because of a force majeure or because of unintentional events the debtor is unable to give or to do something he was obliged to, or because of the same reason has done something forbidden.”

As found in Hofman,²⁴ the phrases “force majeure/*overmacht*” and “unforeseen event” mentioned in Article 1244 and Article 1245 of Indonesian Civil Code, are interpreted by scholars to have the same meaning. On the other hand, Sofwan observes that the difference is that Article 1244 clearly states that in the event of force majeure the burden of proof is laid on the debtor.²⁵ If we compare those Indonesian Civil Code provisions and Article 6:75 of the Dutch Civil Code, it can be perceived that the Dutch Civil Code is more elaborative in giving protection to the parties. In addition to the non fault element on the side of the parties, the Dutch Civil Code also includes the elements of law, juridical act, and common opinion that may excuse a debtor from being liable or may cause a debtor being liable.

Furthermore, there are different of views among Indonesian scholars with regard to whether or not in a legal technical sense, a specific performance is a remedy for breach of contract.²⁶ Sofwan, for example, states that:²⁷

“..., in the situation of *wanprestasi*, the creditor still can demand the fulfillment of prestation before the court with or without damages for losses caused by *wanprestasi*.”

On the other hand, Satrio observes that:²⁸

²²See, Masjchoen Sofwan, Sudewi., Hukum Perutangan, Bagian A, Seksi Hukum Perdata UGM, Yogyakarta, 1980 p. 19 [hereinafter, Sofwan, Hukum Perutangan]; See also, Satrio, Hukum Perikatan, p. 249; Setiawan, Hukum Perikatan, p. 17

²³Translation by Mangunsong, Rany, Indonesian Civil Code, PT. Gramedia Pustaka Utama, Jakarta, 2004, with some modifications referring to the Indonesian version of Burgerlijk Wetboek voor Indonesië, Staatblad 1847:23 translated by Subekti, Kitab Undang-Undang Hukum Perdata, Pradnya Paramita, Jakarta, 2004. [hereinafter Translation by Mangunsong]

²⁴ Hofmann, L.C, Het Ned. Verbintenissenrecht, Part 1, Fourth Edition, J.B. Wolters Groningen-Batavia, 1935, p.60 in Satrio, Hukum Perikatan, p. 249

²⁵ Sofwan, Hukum Perutangan, p.19

²⁶See, Wissink, International Contract Law, p. 99.

²⁷Sofwan, Hukum Perutangan, p. 14

²⁸Satrio, Hukum Perikatan, p. 147

“.. to demand performance is the creditor’s right. Demanding performance and claiming for damages must be distinguished because claiming damages is based on *wanprestasi*”

Similarly, Subekti asserts that:²⁹

“Demanding performance should not be viewed as a sanction resulting from breach of contract. This is because performance is something that the debtor initially agreed to perform.”

The concept of demanding performance is implicitly stipulated in Article 1243 of Indonesian Civil Code. The article provides that:³⁰

“Compensation of expenditures, losses and interests, arising from the unfulfilling of the obligation, will be due if the debtor, after being declared in failure to fulfill his obligation, continues to be in failure, or if the debtor is obliged to give or to do something which can only be given or done within the period that he has passed.”

The phrase ‘after being declared in failure to fulfill his obligation, continue to be in failure’ shows that there is a period for the debtor after the deadline of performance has passed, but before the creditor is entitled to claim damages, to perform on the demand of the creditor. Therefore, it can be concluded that Indonesian Civil Code in this sense has the same concept with the Dutch Civil Code.

Article 1243 of Indonesian Civil Code at the same time states the period when the debtor is considered to be in default. As a comparison, the Dutch Civil Code gives a clearer provision for the term ‘in default’ (*verzuim*). In other words, unlike what is formulated in the Indonesian Civil Code in which the term ‘in default’ is stated together with its consequences, the Dutch Civil Code specifically puts into word the period of ‘in default’, when the default is commenced, including the formality to be taken by the creditor in order to put the debtor into default. Dutch Civil Code puts together these ideas into the following articles. According to Article 6:81:³¹

“Except to the extent that the delay cannot be imputed to him or performance is already permanently impossible, the debtor is in default during the period that the prestation is not rendered, once it has become exigible and the requirements of articles 82 and 83 have been met.”

Article 6:82 provides when a default is in place including its procedures. According to Article 6:82 (1):³²

“Default commences when the debtor is put into default by a written warning granting him a reasonable period for the performance and when there is no performance within this period.”

²⁹Subekti, *Hukum Perjanjian*, p. 53

³⁰Translation by Mangunsong with some modifications

³¹ Haanappel and Mackaay, *Nieuw BW Translation*

³²Haanappel and Mackaay, *Nieuw BW Translation*

There is a condition in which granting the debtor a reasonable period to perform need not be given. That is when the debtor is temporarily unable to perform or if it is evident from his attitude that warning would serve no purpose. In this condition, the debtor may be put into default through a written declaration stating that he is held liable for his non performance.³³ In addition, Article 6:83 serves exceptions in which the formality to put the debtor into default do not necessarily need to be fulfilled. Those exceptions include a condition where a period which has been made available for payment lapses and no performance has been rendered; where the obligation results from an unlawful act or relates to reparation of damage and the obligation is not immediately performed; where the creditor has to presume through his communication with the debtor that the debtor will fail to perform.³⁴

B. Remedies: a comparison between Indonesian and Dutch Contract Law

1. Unitary Concept of Breach of Contract

Dutch Contract Law and Indonesian Contract law adopt the concept of unitary of breach of contract,³⁵ in the sense that the coverage of breach includes all types of failure to perform under obligation of the contract, regardless whether it is caused by a defective non-performance, late non-performance, or no performance at all.³⁶ By virtue of this concept, a creditor is entitled to claim remedies caused by the debtor's breach³⁷ and also the right to set aside the contract. Article 6:265 of the Dutch Civil Code provides that the creditor is entitled to set aside the contract in whole or in part, unless the failure, given its nature or minor importance, does not justify the setting aside of the contract and the consequences therefrom. In case that the performance is not permanently or temporarily impossible, the right to set aside the contract only exists after the debtor is in default. Article 1266 of the Indonesian Civil Code provides for a claim of termination of the contract against the defaulting party. This article also provides that the court could allow a grace period in order to allow the debtor to accomplish his performance.

As compared to the Dutch Civil Code, the Indonesian Civil Code is silent as to claims for termination of a contract due to the debtor's default which will not be given if the failure, given its nature or minor importance, does not justify the termination of the contract and the consequences therefrom. However, the court will refuse to terminate the contract when the court is of the opinion that a termination of the contract will be disastrous to the debtor, while his fault is not deemed so serious.³⁸ The difference among these two codes is that Dutch Civil Code regulates further when the creditor's right to terminate the contract is given while Indonesian Civil Code puts this matter into the court's jurisdiction. Furthermore, Article 1266 of the Indonesian Civil Code provides that the condition for termination is assumed to always

³³Art. 6:82 (2) Nieuw BW, Haanappel and Mackaay, Nieuw BW Translation.

³⁴Article 6:83, Haanappel and Mackaay, Nieuw BW Translation

³⁵ Smits, J.M., *Non-Performance and Remedies in General*, in: Bush, Danny., Hondius, Ewoud., van Kooten, Hugo, Schelhaas, Harriët., Schrama, Wendy, *The Principle of European Contract Law and Dutch Law*, a Commentary, Kluwer International, The Hague, 2002 [hereinafter Smits, *Non-Performance*], p. 326 and Art. 1238 and 1243 Indonesian Civil Code.

³⁶ Id. p325;

³⁷ Art. 6:74 Nieuw BW, Haanapper and Mackaay, Nieuw BW Translation; Art. 1243 Indonesian Civil Code.

³⁸Subekti, *The Law of Contracts in Indonesia, Remedies of Breach*, CV Haji Masagung, Jakarta, 1989, p. 18 [hereinafter Subekti, *The Law of Contract*]

be stipulated in a mutual contract if one of the parties does not fulfill his obligation. In such a case, the contract is not terminated by virtue of the law, but it must be requested to the court. Such request must also be fulfilled, even though the condition for termination due to non-fulfillment of the condition is stipulated in the agreement.³⁹ This provision is waived in contracts in practice, especially if the parties are advised by legal counsel.⁴⁰

2. Non-Performance Caused by the Creditor

The Dutch Civil Code does not explicitly state that non-performance of a debtor is excused if his non-performance is due to the creditor's fault. However, if we observe Articles 6:74 and 6:75 of Dutch Civil Code, such behavior could amount to force majeure.⁴¹ This '*exceptio non adimpleti contractus*' principle does not appear, even implicitly, in the Indonesian Civil Code. However, according to Subekti, this kind of excuse on the part of debtor is generally accepted as valid by courts.⁴² Sofwan, on the other hand, observes that this will be allowed only for a specific contract based on law or based on the content of the contract if found that the one party performance is preceded by, or at least together with, another party's performance.⁴³ This thesis tends to agree with Subekti's opinion because it accepts that one can only claim for performance after he himself has performed his obligations.

3. Fundamental Breach

A breach may be assumed to be fundamental if the breach goes to the root of the contract,⁴⁴ or is sufficiently serious in effect,⁴⁵ as for example in a performance totally different from that which the contract contemplates.⁴⁶ Smits provides three different categories of fundamental breach. The first deals with the strict compliance when the obligation is of the essence, like the provision mentioned in the contract in which the creditor is entitled to terminate the contract for any failure to perform.⁴⁷ The second relies on the gravity of the consequence of the breach.⁴⁸ The third looks at whether the non-performance is due to the intent of the debtor.⁴⁹ The concept of fundamental breach is not recognized in the Dutch Civil Code as well as in the Indonesian Civil Code.

Referring to Article 6:265 of the Dutch Civil Code, the creditor is entitled to terminate the contract in the event of the debtor's non-performance. It is also clear that the abovementioned Article makes available the exemptions in which the right to terminate will not be granted. Taken into account Smits' three categories of fundamental breach, with the

³⁹Translation by Mangunsong with modification.

⁴⁰Gautama, Indonesian Business Law, p. 93.

⁴¹See. Smits, Non-Performance, p. 327

⁴²Subekti, *The Law of Contract*, p. 21

⁴³Sofwan, *Hukum Perutangan*, p. 38

⁴⁴See, *Karsales v. Wallis* [1956]1 WLR 936, in: Beale, *Ius Commune*, p. 503

⁴⁵See, *Suisse Atlantique Societe D'Armement Maritime S.A. v. N.V. Rotterdamsche Kolen Centrale* [1967]1 A.C. 361, 393, 422, in: Beale, *Remedies*, p. 46

⁴⁶Lord Wilberforce in the *Suisse Antique* case at p. 431, in: Beale, *ibid*.

⁴⁷Smits, Non-Performance, p. 330

⁴⁸*Ibid*.

⁴⁹*ibid*.

availability of Article 6:265, the term of fundamental breach does not necessarily need to be provided.⁵⁰ However, from the Indonesian law perspective, in light of Article 1266 of Indonesian Civil Code, in deciding a creditor's claim for termination, the court may use the fundamental breach term as a reference to measure the seriousness of the breach.

4. Withholding of Performance

One thing that is not available in the Indonesian Civil Code is a provision with regard to withholding of performance. Not only is the creditor not entitled the right to withhold his performance based on the debtor's breach; in this situation, he may still be obliged to perform since the court has not yet decided that the contract is dissolved. The Dutch Civil Code, on the other hand, opens the possibility for the creditor to withhold performance as provided in Article 6:262 and Article 6:263. Article 6:262 provides that:⁵¹

“(1) Where one of the parties does not perform his obligation, the other party is entitled to suspend performance of his correlative obligation (2) In the event of partial or improper performance, suspension is only allowed to the extent justified by the failure to perform.”

In addition, Article 6:263 states that:⁵²

“(1) The Party who is obliged to perform first, is nevertheless entitled to suspend the performance of his obligation, if circumstances have come to his attention after the contract was entered into, giving him good reason to fear that the other party will not perform his correlative obligations. (2) In the event that there is good reason to fear that there will be partial or improper performance, suspension is only allowed to the extent justified by the failure to perform.”

The withholding of performance must be terminated if the debtor has furnished security for the performance of his obligation, unless this performance would be unreasonably delayed.⁵³ Smits points out two important notes regarding these articles. First, Article 6:55 ensures that the creditor will still be allowed to withhold performance even after the debtor gives assurance of his performance if performance would otherwise be unreasonably delayed. In this way the concept of protecting the creditor from the possibility of the debtor's fault is an incentive for the debtor to perform and therefore, may have a role in this sense.⁵⁴ Secondly, because Article 6:55 is the species of its genus under Article 6:52 ff., it follows that in the synallagmatic contract this provision does not eradicate the creditor's right to withhold performance.⁵⁵ If we only refer to the correlation between Article 6:55 and

⁵⁰See, Smits, *Non-Performance*, p. 331

⁵¹ Translation by Haanappel and Mackaay, Nieuw BW Translation

⁵²Translation by Haanappel and Mackaay, Nieuw BW Translation

⁵³Art. 6:55 Dutch Civil Code, Haanappel and Mackaay Nieuw BW Translation.

⁵⁴See, Smits, *Non-Performance*, p. 335

⁵⁵Ibid. Article 6:52 provides that: “(1) A debtor who has an exigible claim against his creditor is entitled to suspend the performance of his obligation until his claim is paid, if there is a sufficient relationship between the claim and the obligation to justify this suspension. (2) Such relationship may exist, amongst other things, in the

Article 6:263, the assurance of the debtor to perform will always chase away the fear of the creditor as required by Article 6:263. In this sense, referring to Smits,⁵⁶ it is logically impossible to apply Article 6:55. Therefore, according to Smits:⁵⁷ “The creditor retains the right to withhold performance even after an assurance of performance has been given.”

5. Good Faith Element

Both Indonesian and Dutch Civil Codes require that the obligation of contract must be performed in good faith. The Dutch Civil Code focuses on the parties and their legal relationship in obliging them to perform in conformity with the good faith principle while the Indonesian Civil Code gives a more general notion by putting emphasis on the performance of the contract.⁵⁸ Furthermore, the scope of application of good faith in the Dutch Civil Code is broader than the Indonesian Civil Code as it can be seen from Article 6:2 (2) of Dutch Civil Code. The article states that:⁵⁹

“A rule binding upon them by virtue of law, usage or a juridical act does not apply to the extent that, in the given circumstances, this would be unacceptable according to criteria of reasonableness and equity.”

As compared to the Indonesian Civil Code, the Dutch Civil Code not only requires the parties to perform in accordance with good faith arising from the contract, but also from another source as can be seen from Article 6:248:⁶⁰

“A contract has not only the juridical effects agreed to by the parties, but also those which, according to the nature of the contract, result from the law, usage, or requirement of reasonableness and equity.”

The equivalent of the good faith principle which is absent in Indonesian Civil Code may appear to be that the Dutch Civil Code can extinguish or even exclude the application of the contract and other sources if they are unacceptable according to the criteria of reasonableness and equity.

To ensure the application of the good faith principle, the Dutch judges may have better guidance in case of change of circumstances as compared to Indonesian judges. Article 6:258 (1) of Dutch Civil Code provides that:⁶¹

“Upon the demand of one of the parties, the judge may modify the effects of a contract, or he may set it aside in whole or in part on the basis of unforeseen

event that the reciprocal obligations result from the same juridical relationship or from regular previous dealings between the parties. Haanapple and Mackay Nieuw BW Translation.

⁵⁶ Ibid

⁵⁷ Ibid

⁵⁸ Article 6:2 (1) of Dutch Civil Codes provides that the creditor and the debtor must as between themselves, act in accordance with the requirement of reasonableness and equity. Translation by Haanapple and Mackay, Nieuw BW Translation. Article 1338 para.3 provides that a contract must be performed in good faith. Translation by Mangunsong with modification.

⁵⁹ Translation by Haanappel and Mackaay, Nieuw BW Translation

⁶⁰ Translation by Haanappel and Mackaay, Nieuw BW Translation

⁶¹ Article 258 Dutch Civil Code Translated by Haanappel and Mackaay, Nieuw BW Translation

circumstances which are of such nature that the contracting party, according to the criteria of reasonableness and equity, may not expect that the contract be maintained in an unmodified form. The modification or the setting aside of the contract may be given retroactive force.”

The Indonesian Civil Code does not provide the change of circumstances as an element of good faith. However, in practice the Indonesian Supreme Court has already mentioned this element. For instance, the increase of price of land over the time due to inflation and other factors is considered as the change of circumstances.⁶² Guidance to the application of good faith may also be found in the Article 3:12 of the Dutch Civil Code. The article states that: “In determining what reasonableness and fairness require, generally accepted principles of law, current juridical views in the Netherlands and the societal and private interests involved in the case must be taken into account.” The Indonesian Civil Code is silent concerning this matter.

According to the criteria of the term “unforeseen circumstances,” it is important to note the elucidation provided by the drafter below:⁶³

“The article lays down only one requirement in respect of unforeseen circumstances: they must be of such a nature that the party opposite to the one who demands modification of the contract is not entitled to expect, according to standards of reasonableness and equity, that the contract be maintained unchanged. The requirement will not be easily fulfilled; for reasonableness and equity require in the first place that the parties are true to their word and any deviation from that requirement is a rare exception. The court will have to consider whether the party who expects the unchanged continuation of the contract is just in doing so. There is no need to consider the question whether the said party acts reprehensibly in holding the other to the contract so long as the court has not given a decision against him, for that is not a requirement of this article. Nor does the article require that unforeseen circumstances shall have caused the basis of the contract to be lost (154); even if that is not the case it should still be possible to obtain the revision of stipulation of minor importance of they no longer accord with present circumstances.”

Based on the above statement, an attention is to be directed to the party who does not demand modification of the contract, if he expects that the contract remains unchanged. Notwithstanding the difficulty of the requirement, at least guidance is provided. This is not available in the Indonesian Civil Code.

V. Current Relationship on Oil Palm Production Between Companies and Smallholders

There are some general reasons why oil palm contract farming could not be well implemented. Firstly, smallholders have no bargaining power to negotiate contents of the

⁶² Landrechter Bandung 9 February 1949 no. 179 and 491/1948 Sipil; High Court Jakarta 25 January 1952 no. 76 and 76a/1949, See, Satrio, *Hukum Perjanjian*, pp. 366-7

⁶³ Drion, J., de Grooth, G, de Jong, F.J., in: *The Netherlands Civil Code, Book 6 The Law of Obligation, Draft Text and Commentary*, Translated by Drion-van Rooyen, E.J., and van Dijk, R.H., Edited by The Netherlands Ministry of Justice, Sijthoff-Leyden, 1977, pp. 582-583 [hereinafter, de Grooth Draft Text and Commentary]

agreement with the companies, the economically powerful companies.⁶⁴ In this condition, smallholders are in no chance to reject the contract proposed by companies.

The incompleteness of the contents of the contract will give more space for the stronger party, companies, to enforce their power taking advantage of smallholders, the weaker party. In the uncertainty of production and the market and the worsen inflexibility for smallholders to shift from one commodity to another commodity may make their bargaining power even weaker.

Smallholders lack of basic technical capacity to implement the required agronomic practices.⁶⁵ At the other side, smallholders sometimes only have little access to find technical assistance, farm inputs such as planting material and fertilizers, and finance either from companies or from the government.

Smallholders can also lack entrepreneurial skills or an entrepreneurial attitude, which may result in them reallocating resources for consumption purposes (e.g. fertilizer stocks are sold for cash income) while they were designated for farm management.⁶⁶ A closer and continuous relationship through intensive communications between companies and smallholders may help to reduce to a minimum level these lacks.

Contract farming in the oil palm industry has also brought benefit to smallholders. According to Chayadia and Waibela,⁶⁷ the benefits of the Indonesian oil palm industry for smallholders are mainly because: “ firstly, the contract provides smallholders with quality seeds and advanced planting techniques in establishing the smallholders’ plasma oil palm plot. Secondly, the contract smallholders benefit from the higher price as set in the contract during the survey year. Thirdly, contract farmers have higher net revenue per hectare in spite of higher production costs induced by the improved production technology.”

When smallholders form a cooperative among them to contract with company, capacity building is one of the most important things to do in order to be successful⁶⁸. This leads to a strong interdependence of individual smallholders and a social pressure that encourages all members to implement best practices.⁶⁹

In the form of cooperatives, smallholders may have a better bargaining power against the company. The cooperative also will find easier to get technical assistance on a range of issues, by the cooperative itself as well as the company. Loan facilities from banks may also be easier to get, while fertilizer and transportation to bring crop to the mills can also easily be got from the company. In short, mutual benefits for the smallholders and the companies will easily be achieved when the smallholders form cooperatives.

Below is the example of a farming contract between an agricultural state owned company and smallholders (households), witnessed by a bank as the loan provider of the project, namely a Partnership Agreement;⁷⁰

⁶⁴ Erkan Rehber, 2007, *Contract Farming, Theory and Practice*, The Icfai Universtiy Press, p. 104

⁶⁵ Oxfam Discussion Paper, *Ibid.* p. 15

⁶⁶ *Loc.cit.*

⁶⁷ Cahyadia, Eko Ruddy, Waibela, Hermann Waibela, 2011, *Do Smallholders Gain from Contract with an Oil Palm Company? Lessons Learned from Jambi, Indonesia*, Conference on International Research on Food Security, Natural Resource Management and Rural Development, University of Bonn, p. 4

⁶⁸ Oxfam Discussion Paper, *Op.cit.* p. 24

⁶⁹ *Op.cit.* p. 40

⁷⁰ The Contract is permitted to be put in this paper but it is suggested that the name of the parties and locations are being hidden.

“PARTNERSHIP AGREEMENT BETWEEN**COMPANY****AND****KOPERASI UNIT DESA...****KECAMATAN....., REGENCY****WITH REGARD TO THE PROJECT DEVELOPMENT AND MANAGEMENT OF OIL PALM PLANTATION BY PARTNERSHIP SCHEME****AT ... DITRICT, REGENCY, ... PROVINCE**

Today, , each party who undersigned below:

- I.: Acting as Director of PT.... (Company) resided in, established based on a notary deed,, S.H., in Jakarta No.... on, year.. and together with all the beneficiaries and all of their rights and obligations hereinafter is called as:

FIRST PARTY

- II. Head of Koperasi Unit Desa (KUD) resided in.... District,Regency,.... Province, established by a Legal Entity Number....., acting for and on behalf of the Member of Koperasi Unit Desa (KUD)....., hereinafter is called as:

SECOND PARTY

Herewith the above-mentioned parties agree to make and sign the partnership agreement with regard to the development and management of Oil Palm Plantation Project in the form of a partnership scheme atDistrict, ... Regency, Province, which source of funding will be from KKPA credit facility of one of the Banks; Moreover the PROJECT will be granted from the COOPERATIVE to its member, hereinafter is called as COOPERATIVE MEMBER, by establishing the rules and requirements as stipulated below:

Article 1**PROJECT LAND ACREAGE AND LIST OF COOPERATIVE MEMBER**

1. The sum of land acreage required in this PROJECT is 14,000 hectare, which is equal to 7,000 households; all of which will be used for planting the oil palm.
2. BOTH PARTIES and Regional Government (Pemda Tk. II....) conduct the selection of the COOPERATIVE MEMBER who will be participating in the PROJECT as provided in this agreement and to include the name list of members with their photograph.
3. The COOPERATIVE MEMBER who will be participating in the PROJECT are people of the region projected to be the PROJECT acreage, which is categorized as the potential land and have fulfilled the technical requirements for oil palm plantations, and those who could evidence the originality and validity of their land right.

Article 2

OIL PALM PLANTATION DEVELOPMENT AND MANAGEMENT AND TRANSPORTATION/SALE/PURCHASE OF FRESH FRUIT BUNCHES (FFB)

The SECOND PARTY appoints and gives its power to the FIRST PARTY to develop and manage the 14,000 hectare oil palm plantation, from the first step until the transfer of the farm to each COOPERATIVE MEMBER which include the activities:

- a. Surveying and land mapping;
- b. Land clearing;
- c. Seedling bed;
- d. Planting the seeds which are approximately twelve months old or seeds that are technically appropriate to be planted, including the seeds that are reserved for insertion ("*sulaman*");
- e. Maintenance of the palms up to the end of the third year, since the planting phase with mandatory amount to be met is 128-130 palms per hectare, 126 palms per hectare minimum;
- f. Building and maintenance of roads and bridges prior to transfer to the COOPERATIVE MEMBERS;
- g. Obtaining legal ownership of the MEMBER COOPERATIVE's land (land certificate)

The FIRST PARTY as the appointed party and beneficiary of the COOPERATIVE who develops and maintains the plantation, will give priority to the COOPERATIVE MEMBERS to be employed and paid with the minimum regional wage in accordance with the applicable Governmental Regulation and rules applied in the company of the FIRST PARTY until the palms are being converted.

The SECOND PARTY is obliged to sell and the FIRST PARTY is obliged to buy FFB harvested from the COOPERATIVE MEMBER's plantations. In the event the COOPERATIVE MEMBER sells its FFB to the third party other than the FIRST PARTY, there would be a sanction imposed in accordance with the applicable regulations.

The SECOND PARTY is obliged to hand over FFB to the FIRST PARTY's Oil Palm Plant (OPP) as has been specified and the FFB's transportation cost is borne by the SECOND PARTY.

Article 3

PROJECT COST

All costs incurred from the Plantation PROJECT i.e. the administration of activities stipulated in Article 2 (1) will be evaluated by the Bank.

Each MEMBER COOPERATIVE who participated in the PROJECT will be charged with insurance fee Rp. 250,000 per hectare as their credit guarantee.

Article 4

NUCLEUS PLANTATION AND PALM OIL PROCESSING PLANT

The FIRST PARTY is under obligation to build a Nucleus Plantation as an exemplary plantation and Palm Oil Processing Plant to accommodate and process the COOPERATIVE MEMBER's harvested palm products.

Article 5

CREDIT PROPOSAL

The SECOND PARTY proposes a loan agreement to the Bank in accordance with Bank applicable rules supplemented by the cooperation agreement between the FIRST PARTY and the SECOND PARTY.

The FIRST PARTY is under obligation to guide and assist the SECOND PARTY in fulfilling the credit requirements required by the Bank.

Credit facility provided by the Bank for the SECOND PARTY will be paid through the FIRST PARTY in accordance with the cooperation agreement between the FIRST PARTY AND SECOND PARTY based on its physical progress.

Article 6

CREDIT FACILITY'S DISBURSEMENT AND UTILIZATION

The FIRST PARTY is acting as a developer of the SECOND PARTY's plantation.

The FIRST PARTY appoints a personnel who acts as a field staff and is responsible to make a report on the project's physical progress.

Article 7

CREDIT FACILITY

Credit facility requested as stipulated in Article 5 that has been approved by the Bank is used for plantation development through the FIRST PARTY.

Article 8

PLANTATION MANAGEMENT

In the plantation development phase, management of plantation is the responsibility of the FIRST PARTY.

In the event there is still outstanding credit, the SECOND PARTY along with its members is responsible for the plantation management including payment of operational cost and production, in addition to repayment of the credit facility (i.e. principle, interest and other liabilities)

Article 9

PLANTATION MANAGEMENT AFTER THE END OF LOAN AGREEMENT

Once the credit has been fully paid, the COOPERATIVE MEMBER under the coordination of the SECOND PARTY is responsible for the plantation management including payment of operational cost and production.

All of the plantation products owned by the COOPERATIVE MEMBER in the form of FFB still have to be sold to the FIRST PARTY through the SECOND PARTY.

The FIRST PARTY is still under obligation to give supervision, technical guidance and management to the COOPERATIVE MEMBER.

Article 10

TRANSFER OF PLANTATION

Transfer of plantation from the FIRST PARTY to the COOPERATIVE, which is later to be handed over to each of the COOPERATIVE MEMBER, is carried out by following the plantation transfer provision set out by the government.

In order to achieve an optimum result, after the transfer of plantation to the COOPERATIVE MEMBER, the FIRST PARTY guides and supervises the COOPERATIVE MEMBER with regard to oil palm technical cultivation and its management.

Article 11

LOAN REPAYMENT

1. The COOPERATIVE MEMBER source of funding to fulfill all of their obligations towards the COOPERATIVE in the form of principle, interest and other liabilities (hereinafter referred to as INSTALLMENT), which have to be paid by the SECOND PARTY through the FIRST PARTY to the Bank is as much as 30% from the selling of their FFB.
2. Fulfillment of all obligations as stipulated above are conducted by the FIRST PARTY by transferring to the Bank from the account of the COOPERATIVE MEMBER, which is from their FFB sales deduction.
3. The Bank will give the COOPERATIVE MEMBER their installment payment receipts for the implementation of provision stipulated in this article point 2.

Article 12

FFB PAYMENT TO THE COOPERATIVE MEMBER

1. The FIRST PARTY is in charge of the FFB purchase payment to the COOPERATIVE MEMBER by deducting all of their liabilities before hand.
2. The place of FFB purchase and payment of the FIRST PARTY to the COOPERATIVE MEMBER is carried out in the nucleus plantation in accordance with the consensus between the FIRST AND SECOND PARTY.
3. FFB pricing is set out based on the government decree in effect at the time.

Article 13

REPLANTING FUNDS

The SECOND PARTY is obliged to open a Savings Account for Replanting Funds at the Bank or financial institution non-bank that has been appointed by the SECOND PARTY in order to hold the replanting funds. The SECOND PARTY's obligations with regard to these replanting funds:

1. Prior to loan settlement the amount of contribution towards replanting funds is 2.5% of farmer's gross income; and
2. During post loan settlement the amount of replanting funds is 2.5% of farmer's gross income.

Article 14

DEVIATION

In the event the COOPERATIVE MEMBER leaves the plantation area, which will lead to failure in fulfilling its obligations toward the SECOND PARTY, the SECOND PARTY is obliged to take over that member's plantation and also to carry out obligations attached to it.

Article 15

COOPERATIVE'S SUPERVISION AND DEVELOPMENT

The FIRST PARTY is under the obligation to supervise and develop the SECOND PARTYS's business, which aims:

1. To increase the participation of the COOPERATIVE MEMBER in the form of skills, disciplinary, and responsibility towards all of the agreements that have been made on the basis of the partnership principle;
2. To enhance the sense of awareness in cooperating between the COOPERATIVE MEMBER, the SECOND PARTY, the FIRST PARTY, the Bank, and the other partners. This kind of cooperation is being realized through increasing the knowledge and skills so that optimum productivity can be achieved;
3. To strengthen and set out the organization and the SECOND PARTY's business management in order to achieve effectiveness, so the rules are stipulated below:

- a. A group meeting is held regularly, which is attended by technical manager/its deputy of the FIRST PARTY as a media for cultivation technology transfer using a socialization method;
- b. A meeting for the FIRST PARTY, the SECOND PARTY and the COOPERATIVE MEMBER is held regularly and as needed.

Article 16

MANAGEMENT FEE AND OVERHEAD COST

The FIRST PARTY is entitled to receive Management Fee and Overhead Cost by 5% of the value of crop and non-crop investment from the SECOND PARTY.

Article 17

DISPUTE SETTLEMENT

1. Any disagreement or dispute arises out of or related to the implementation of this agreement will be settled by the parties amicably (*musyawarah*);
2. If through the amicable mechanism the parties are unable to reach an agreement, any disagreement and/or dispute will be resolved through the assistance of District's Regional Government.
3. If both parties cannot accept the decision of Kendari District's Regional Government through forum, then any disagreement and/or dispute shall be resolved through District Court.

Article 18

ADDENDUM AND DOMICILY

1. Things that are not regulated and/or have not been adequately provided for in this agreement will be governed jointly by the parties in an addendum, which becomes an inseparable part of this agreement.
2. With regard to this agreement and the consequences that may arise, both parties agree to a common domicile and remain in the local District Court Clerk's Office where the collateral is located, without prejudice to the Bank's right to file a lawsuit from the other district courts within the territory of the Republic of Indonesia.

Article 19

CLOSING

This agreement shall take effect from the date signed by the parties and concluded when all of the debt and liabilities of the SECOND PARTY to the bank have been paid off well and/or at the time of the end of one cycle of planting oil palm plantations, which is approximately 25 years.

This partnership agreement is made in four copies with each two of which are provided with the necessary stamp duty, so that they have similar legal effect for each party.

Name of City,

Company

KUD

Director

Leader

PT BANK

Marketing Director”

VI. Analysis of The Contracts

The two above mentioned contracts will be analyzed in this paper. The first is the standard contract namely Partnership Scheme Contract⁷¹ and the other a real contract namely Partnership Agreement between a state owned company and cooperative.

A. Standardized Partnership Scheme Contract

The contract was drafted in a very short and general form. It seems that the drafter has no strong political will to protect farmers through the standard of contract. The term mentioned on the Art. 1 Section (2a) reflects that the Company shall have the right to reject raw materials sent by Smallholders when incompatible with the standard which was agreed. It is recommended, when there is a strong willingness from the government to use the standard of contract as means to protect smallholders, that the drafter provide the possibility for the Company to reduce price of non performing goods delivered instead of their rejection. It is also an issue that the standard of contract does not mention whether the non performing raw material achieved is fundamental or not.

At the other side, the obligation of Smallholders is drafted to be so strict. Due to Art. 1 Section (3b), for example, Smallholders are obliged to make appropriate cultivation technique comply with technical standard so as to generate good quality of raw materials. It is not mentioned in a more detailed manner what was meant by "good quality" of raw material. With this very general term, it is possibly easy for the Company to take a good reason to reject the good, and in the worse market situation, use the general term as "good quality" of raw material.

B. Partnership Agreement for Oil Palm Production

The contract was between state own Company and Cooperative, in which 7,000 smallholders are involved on it over 14,000 hectare of land. The land owners were the Smallholders with the obligation on them to show the evidence of land ownership.

The project of Oil Palm Cultivation, will be financed through the KKPA Program (Members' Primacy Credit Cooperative) provided by Bank. After the Cooperative receives the project, the Cooperative will pass the project to its members.

Rights and obligations among the parties seem to be equal. The Company is obliged to prepare and clear the land, provide seed and planting it for approximately twelve months or provide seeds that are technically appropriate to be planted, and maintaining the land, provide building and maintenance of road and bridges, and obtain a land certificate for cooperative's members.

On the other side, the obligation of the Smallholders are to sell the FFB (Fresh Fruit Bunch) to the Company who is obliged to buy it. In the event the cooperative member sells its FFB to the third party other than the Company, there would be a sanction imposed in accordance

⁷¹ The standard of contract is obliged to be followed by the Regulation of MoA Number 98 of 2013, Annex II.

with the applicable regulations. The Cooperative is obliged to hand over the FFB to the Company's Oil Palm Plant (OPP) as has been specified and the FFB's transportation cost is borne by the Cooperative.

It was the Cooperative who borrows money to fund the project. Payments of the loan would be taken from 30% of the sales of FFB, paid by Cooperative through Company. The loan would also be paid to the Cooperative members through Company.

The important aspects of the contract that usually need to be carefully mentioned are absent from the contract. That is in the event of default and its consequence. The contract only prevents that a situation in which the Cooperative member leaves the plantation area, which will lead to failure in fulfilling its obligations toward the Cooperative, the Cooperative is obliged to take over that member's plantation and also to carry out the obligations attached to it.

It seems the contract leaves the lack of event of default on the dispute resolution, primarily based on the so called "musyawarah" or deliberation, that is to settle the dispute by the parties amicably. Whenever they fail to resolve their dispute, settling it before the district court might be done after the efforts of the Regional Government have also failed to resolve it.

This lack of provision with regard to events of default makes the contract have a significant weakness. It has to be noted that the position of Smallholders in general is always weaker although better because they are now the members of the Cooperative which may increase their bargaining position. Furthermore, because the payment of the loan to and from the Cooperative members can only be done through Company, this would even weaken the position of the Smallholders.

Last but not least, the contract did not mention any provision with regards to supervening events. When those events occur, parties must be brought into what is available in Indonesian Contract Law which regulates the matter in a very general manner and only contains force majeure. Hardship and frustration of purpose are not recognized by Indonesian Contract Law.

VII. Conclusions

Due to the lack of bargaining power of the Smallholders in the Partnership Scheme Contract, in general, it can be concluded that without carefully drafting the contract, protection to them seems to be minimal. The lacks of Smallholders are almost in every aspect like capital, expertise, accessibility to production and market, and their position in the monopsony market structure.

Government through its regulation tried to protect Smallholders, but the protection is given through the opportunity for them to enjoy the industry of oil palm in which the Company in order to get license of IUP, IUP-B and IUP-P have to involve Smallholders. The government does not give sufficient protection through the standard of a Partnership Scheme Contract that has to be made by Smallholders and Company.

Contracts that are made by parties also need to be improved. The main lack of the contract is the absence of complete provisions regarding to the “event of default” and force majeure.

To strengthen the bargaining position of Smallholders, encouraging them to form Cooperatives may increase their bargaining position in many aspects like fund, capital, technology, and market access.

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**Promoting Good Contract Practices
between Producers and Buyers
in Contract Farming Operations in the Asian Context**

**THE LEGAL DIMENSION
OF CONTRACT FARMING**

**Consultation Workshop on the UNIDROIT / FAO Legal Guide
on Contract Farming**

Bangkok, 26 September 2014



Overview of the Legal Framework of Contract Farming for Producer-Buyer Relationships in Cambodia

by

Prasnar Yi¹

CONTENTS

INTRODUCTION

I. CORE LEGISLATION RELATED TO THE CONTRACT FARMING

- 1) The general principles of contract
- 2) The special legislation related to agriculture
 - a) The Sub-Decree on Contract Farming
 - b) The Law on Establishment of Agricultural Communities
 - c) Draft Law on Agriculture Land Management

II. COMPLEMENTARY LEGISLATION ADDRESSED THE MAIN CONTRACT FARMING ISSUES

- 1) The importance of series of contracts around the “contract-farming”
- 2) Some examples of surrounding laws
 - a) The Labor Law
 - b) The Insurance Law

CONCLUSION

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The Henri Capitant of Cambodian Law Association works particularly with legal professional, judges and authorities on the Civil Code annotation for a good utilization of it by proposing ways to fully use this Code. The Association works as well on the other legal texts and other relevant juridical tools in Cambodia to contribute to harmonize and modernize Cambodian law. The Association is then involved in findings for a well-balanced relationship in contract farming.



INTRODUCTION

In France, contract farming is legally defined as an “*integration contract*” in agriculture. It is characterized by a single decision-making center, who heads both the production and the processing and marketing of processed products². The law protects the farmer in regulating this type of contract known as “*agricultural integration contract*”. Furthermore, it seems that the contract farming, involving diverse contracts, is a *sui generis* type as the contract imposes on the producer not only an obligation to perform but also an obligation to act in a pre-defined way³. One main characteristic of this contract is to put the farmer in a state of economic dependency. This contract accomplishes actually the “*integration*” of the farmer’s activity in the industrial trader’s, because it imposes a discipline of its production, its supply or sales.

In Cambodia, with 80% of rural population, the Royal Government mindful of the important role of agriculture in poverty reduction and economic growth⁴, has included agriculture in the top priorities in its national policy⁵. Alike in other developing countries, notwithstanding benefits and opportunities accessible by contract farming, Cambodia is aware that the relationship between producers and buyers shall be established by clear provisions⁶. The Cambodian Department of Agro-Industries of the Ministry of Agriculture, Forestry and Fisheries (MAFF) fully understands the issue of possible unbalanced relationship between producers and buyers in contract farming: a process of reflection is under way and legal measures are being setting up.

As mentioned in the abstract of Unidroit/FAO Legal Guide on Contract Farming, contract farming parties will be subject to a number of Cambodian laws and regulations that will influence other elements of the contract. These involve “*the regulatory protection of human rights in agriculture, food safety and the protection of animal and plant health and the environment; decent rural employment in agriculture; laws governing the access to natural resources necessary for agricultural production contracts; and the access to agricultural inputs and the trade of agricultural products*”⁷. However, as part of this contribution, we will only mention a number.

This paper aims to present an overview of the legal framework of the contract farming in Cambodia with the core legislation in force (I) and the complementary legislation applicable which addresses in particular the concerns from civil society⁸ (II).

² Ibid.

³ *Contrat d'intégration en agriculture*, §3 - Nature juridique, Jacques PRÉVAULT, Professeur of Law, January 2012

⁴ *Cambodia's Agriculture: Challenges and Prospects*, Cambodian Institute for Cooperation and Peace Working paper No 37, by Sok Siphana, Chap Sotharith, Chheang Vannarith

⁵ National Strategic Development Plan 2009-2013 (“improving agricultural productivity and diversification”); Strategy for Agriculture and Water 2010-2013; policy paper on the Promotion of Paddy Production and Rice Export 2011-2015.

⁶ The plurality of terms that describe the parties of contract farming shows how the contractual relationship can vary and should be clarified – the contracting farmer is called “producer, farmer, producer organization, agricultural producer or market operators”, while the buyer is called “contractor, purchaser, food processor, exporter, retailer, trader, distributor or wholesaler”.

⁷ *Abstract of Unidroit/FAO Legal Guide on Contract Farming*, UNIDROIT 2014, Study S80A – Doc. 17, February 2014, 18 p.

⁸ *NGO Forum on Cambodia Comments on the Sub-decree on Contract-based Agricultural Production (Contract Farming)*, expressed in a statement dated July 29, 2014.



I. CORE LEGISLATION RELATED TO THE CONTRACT FARMING

In contract farming, the legal sources governing the relationship between producers and buyers are led, first, by the general principles of contract defined in the Civil Code and, second, by special legislations related to agriculture.

1) The general principles of contract

The Civil Code, legal ground of private law including the principles of general contract law, defines the core legal issues of contract, from its formation to the resolution of conflicts, including its content, its effects, its performance or non-performance.

As general principles, the Civil Code mentions the prohibition of abuse of rights⁹ or the principle of good faith¹⁰: “*rights shall be exercised and duties performed in good faith*”. The principle of freedom of choice also called “*principle of the autonomy of the will*” or “*principle of party autonomy*” (“*principe de l'autonomie de la volonté*” in French) expresses that “*a contract is the matching of intentions held by two or more parties to create, change or extinguish an obligation*” and that “*an obligation arising from a contract (...) shall be an obligation created based on the intention of (...) both parties*”. This condition is susceptible to become a legal issue in the situation where the buyer/trader establishes and supports the farmer's organization¹¹.

As in most developing countries, contract farming tends to be unequal to the detriment of smallholders with lacks of information and in weak economic position vis-à-vis buyers in stronger situation firms who may want to impose their provisions as they are almost in monopsony position. For a fair relationship between parties, the Civil Code prevents the stronger party to receiving excessive benefits from the weak party, pushed to accept all conditions: “*Should a party enter into a contract while taking advantage of the other party's economic difficulties, ignorance or inexperience, and receive excessive benefits from said contract, the counter-party may rescind the contract on the grounds of defect in the declaration of intent*”¹².

The Cambodian legislation is no exception regarding the supremacy of public order and moral which limits the principle of party autonomy. All provisions of contract which contravene “*law or public order and good morals*” shall be deemed as void. Moreover, if the producer uses employees, he shall comply with the labor law and human rights principles as set out in the preamble of the Cambodian Constitution. Even to increase his productivity, the producer shall not harm the environment.

Although both parties are bound by their mutual obligations, there is an exception to this general rule¹³: “*If performance of an obligation has become impossible without the fault of the obligor, the obligation shall be extinguished and the obligee may not demand performance thereof*”¹⁴. However, this provision is not clear with the circumstances constituting an exonera-

⁹ Civil Code, article 3, unofficial translation.

¹⁰ Civil Code, article 5, unofficial translation.

¹¹ Formulation of an Agro-Industry Strategic Development Plan, Annex A5 Contract Farming; Review of Some of the Many Issues Involved, FAO and The Department of Agro-Industries of the Ministry of Agriculture, Forestry and Fisheries of Cambodia, highlighting many of the issues involved with contract farming given potential importance for stimulating agro-industrial development across large sectors of rural communities in Cambodia, 2010.

¹² Civil Code, article 351, unofficial translation.

¹³ Civil Code, article 415, unofficial translation.

¹⁴ Article 31, unofficial translation.



tion of responsibility. In France, the cases exonerating responsibility of the obligor are the force majeure (or unforeseeable circumstances) or an unpredictable and irresistible impediment due to a third party. Traditionally, the criteria constituting a force majeure are unpredictability, irresistibility and externality. Force majeure is a legal concept developed by the jurisprudence. In France, this qualification is made by the jurisprudence of the Supreme Court¹⁵, but in Cambodia it is difficult to predict the court's decision. Is a violent storm or a labor strike can justify an exoneration of responsibility preventing the producer to fulfill its obligations as a force majeure does?

2) The special legislation related to agriculture

Cambodia has not a code of agriculture yet. The development of legal and regulatory framework related to agriculture is only at its beginning. But mindful of the importance to enhance the agriculture sector, the MAFF has started to draft and set up some key laws and regulations related to agriculture.

The special legislation related to agriculture impacting contract farming is expressed by:

- the Royal Decree on the Establishment and Functioning of Agricultural Cooperatives, Union of the Agricultural Cooperatives and the Pre-Agricultural Cooperatives adopted in July 2001,
- the Sub-Decree No. 15 on Phytosanitary Inspection adopted in March 2003,
- the Law on the Management of Crop Species and the Rights of Crop Breeders adopted in June 2008,
- the Sub-Decree on Contract Farming adopted in February 2011,
- the Law on Establishment of Agricultural Cooperative adopted in May 2013 and
- the draft Law on Agriculture Land Management.

For the relationship issues between producer and buyer in contract farming topic, we will focus only on the last legal texts which are the most recent and relevant.

a) *The Sub-Decree on Contract Farming*

The Sub-Decree on Contract Farming provides provisions relating to the implementation framework of the contract farming, called “*contract-based agricultural production*”, the roles and responsibilities of the State (“*bridge investors and farmers, producers, processors in the framework of contract-based Agricultural Production*”), the obligations of producers, the obligations of purchasers, and also to resolution of conflicts.

Whereas the Civil Code states the freedom of choice (*principe de l'autonomie de la volonté*) as an essential principle by all forms of contract – “[a] contract is the matching of intentions held by two or more parties to create, change or extinguish an obligation”¹⁶; “[a] contract comes into effect when an offer and an acceptance thereof conform to each other”¹⁷ –, the Sub-Decree limits this freedom by setting out that “[t]he contract of contract-based agricultural production shall be in written format and be authentic letter”¹⁸.

The sub-decree specifies an “*Institution and Coordinating Mechanism*”, dedicated to the roles and responsibilities of the State. It also defines a coordinating committee called “*contract-*

15 Case law, French's « Cour de Cassation », February 4th 1983

16 Civil Code, article 311, unofficial translation.

17 Civil Code, article 336, unofficial translation.

18 Sub-decree on Contract farming, article 10, unofficial translation.



based agricultural production committee¹⁹, composing of members from several ministries and headed by the MAAF, has been established. The coordinating committee is responsible to “*intervene and reconcile conflicts and problems arising from Contract-based Agricultural Production which could not be solved by the competent institution or any conflicts requiring inter-institution resolution*”. Actually, the important role of the committee is only coordinating and reconciling both parties and could not render a resolution.

Regarding the obligations of the producers and the buyers, both parties have the obligations to comply with conditions as inscribed in the contract. The buyer shall clearly specify the commodity items such as quantity, quality, place, and date of delivery and acceptance of the commodities; provide agricultural materials and technical services; and provide credit advance. In counterpart the producer shall proceed production activities based on seasonal and required timeframe; supply on time, in term of grade, quantity, and quality and due timeline; accept the payment of product value as set in agreement. In the contract farming operation, the parties, especially the farmer, expect to have made a deal on a long period of time, because the investment is important. But paradoxically, the contract farming is usually concluded for a short period and subject to renewal. The fact that the determination of price and quantity is not set clearly yet, could weaken the farmer who expects to maintain a minimum of price and quantity because of its obligation to pay the credit he contracted in this operation. In France, a framework contract (“*contrat-cadre*” in French) is usually concluded by parties to mitigate this.

Additionally the sub-decree sets out the dispute resolution mechanism²⁰ by indicating that any dispute relating to the implementation of the contract farming shall be resolved amicably in accordance with the conditions provided in the contract. In case of failure of amicable resolution, the dispute could be resolved at the will of parties by pursuing the mechanism stated in the sub-decree. Therefore, the parties could agree for any resolution (negotiation, meditation, judicial system or arbitration) without appealing the coordinating committee.

b) The Law on Establishment of Agricultural Communities

The Royal Government of Cambodia “*encourages the formation of associations, agricultural communities, or agricultural organizations as the bases to develop contract-based agriculture*”²¹. Following this policy, the Law on Establishment Agricultural Communities promulgated in June 2013 allows farmers to organize themselves in legal cooperatives, and establishes agriculture communities, unions of agriculture communities, and the alliance of agriculture communities. This law defines an agriculture community as a private legal entity functioning as an establishment for agricultural economy.

c) Draft Law on Agriculture Land Management

A law on agriculture land management has been being drafted since 2011 (initially called “*Law on the Use and Management of Agricultural Land*”). The draft has been recently updated in May 2014 after several reviews and comments from CSOs/NGOs. This law should define the framework for the management, use, and development of agriculture and land used for agriculture in Cambodia. It should ensure the sustainable management of agricultural land, to increase

¹⁹ Sub-decree on Contract farming, article 7, unofficial translation.

²⁰ Sub-decree on Contract farming, article 11.

²¹ Sub-decree on Contract farming, article 4.



productivity of agricultural land and to protect the environment. A full chapter is also expressly dedicated to contract farming issues.

II. COMPLEMENTARY LEGISLATION ADDRESSED THE MAIN CONTRACT FARMING ISSUES

Contract farming, governed by the laws and regulations which have been presented, however, is not by itself able to achieve economic operation which justifies its conclusion (the cause of the contract). A group of contracts is then, necessarily, forming around that contract to support achieving the contract farming operation (1). These contracts, altogether called “the series of contracts”, are subject to a series of additional laws (labor law, insurance law, commercial enterprise law) which should be present for providing a comprehensive Cambodian legal framework on the issue of contract farming (2).

1) The importance of series of contracts around Contract farming

The series of contracts around the “contract-farming” are very important since either they have the same object either they contribute to the achievement of the same transaction (here the contract farming operation) and are united by identity of cause (the sense of common purpose). It should be noted however, that this series of contracts is heterogeneous in the sense that it consists of contracts with different natures.

There are diverse interests in clarifying the series of contracts ‘issues. For example, what is the incidence of the invalidity or rescission of a contract on the other contracts in the series of contracts? Are these contracts must be subject to a holistic and comprehensive interpretation, that is to say, be interpreted in relation to the economic operation they perform?

By way of illustration:

Contract of employment – A farmer tends to sign labor contracts with employees, whether a written contract is formally concluded, only for a period which may not go beyond the duration of the “contract farming”. The Labor Code prohibits the indefinite renewal of fixed-term contracts and will re-characterize the contract as a permanent contract or open ended contract.

Contract of Insurance – The activity of the farmer, party to the “contract farming” should require to be covered by an insurance in order to prevent it from falling into endless circles of debts, especially in case of bankruptcy, because it is expensive for the farmer who invests for several years and beyond the duration of the first “contract-farming”.

Lease Agreement – If the farmer rents a plot of land for the contract farming operation, the lease agreement can affect the operation.

A framework agreement would be useful for parties to the contracts of the series of contracts to have a better view of the potential impacts from the other contracts in this series. It will allow them to better manage their expectations. It can be helpful to enclose the contract farming in a framework contract in order to facilitate the holistic and comprehensive interpretation of the permanent contract of employment having regard to the contract farming operation.



In France, the law requires that the parties clearly express their intention to make these contracts interdependent together, even indivisible, to qualify the series of contracts²². The contract farming in Cambodia may also contain clauses in that sense.

2) The surrounding laws

The contracts from the series of contracts, which has just been brought to light, are subject to other laws and other legal instruments, such as the Labor Code or the law on insurance.

a) *The Labor Code*

In the 1990s, the Cambodian authorities requested the French Ministry of Labor to develop a new Labor Code. French experts, whose role was decisive, were then sent to work with officers from the Cambodian Ministry of Labor and draft the new Labor Code. It will be adopted in 1997. The text reflects the desire of the Cambodian legislature to respect and implement the fundamental conventions of the International Labor Organization (ILO) that Cambodia has ratified, including enshrining the principles of equality and prohibiting discrimination in labor relations, promotion of equal pay, eradication of child labor and forced labor. The Labor Code does not break with the past, and expresses a compromise by fitting both with the market economy and one where the State is interventionist. It pays special attention to the plantations in a chapter on special conditions of work in agricultural occupations²³. These rules aim to protect a working population isolated in large farm²⁴.

In general, the Code prohibits employers from discriminating particularly in pay between men and women²⁵. It gives women a social protection: they are entitled to receive social security and other social benefits as determined by law. In terms of access to employment and occupation, they have a general protection²⁶. The Code clearly prohibits child labor, minimum age being 14 years. For issues relating to the health of employees, the Labor Code establishes a compulsory general insurance scheme²⁷ for accidents at work and the law of 2 October 2002 on the social security system and its implementing decree 2007 formally materialize this obligation.

b) *The draft law on insurance*

Cambodian insurance law is being revised to better meet the current need from the market. A draft law being adopted enriches the existing legislation and establishes a number of facilities for

²² Case law, French's « *Cour de Cassation* », April 1st 2006

²³ Labor code, articles 193-226

²⁴ The first important rubber plantations in Cambodia, which are still in use and dating back to 1925, will experience a boom rapidly with the development of the automobile and its tires. The first comprehensive text to regulate the terms and use of manpower goes back to March 9, 1910. Plantations in general, which also apply to other crops such as coffee, pepper and tropical fruits easily exportable, require heavy investments that rely on large economic groups. Cambodian law makers have set out very early a strict framework for protecting working relationships and conditions in this activity area, specifying the limits of different characteristics: recruitment conditions, proper working conditions (working hours, wages, features and limitations of the work of women and young people), living on the plantation. In the early 2000s, the rubber industry represents 70,000 hectares, which cover 45,000 are planted areas with 45,000 tonnes produced. Cambodia is the 14th largest in the world. Production of Cambodia is divided among seven large plantations which employ 12,000 people and those of family size which generally call for manpower from outside.

²⁵ Labor code, articles 106

²⁶ Labor code, article 12

²⁷ Labor code, article 256



the farmer, party to the contract farming, including the possibility to access to small scale insurance and coverage in case of bankruptcy.

CONCLUSION

The legal framework for implementing the contract-farming operation is developing and is enriching. However, it is necessary to consider the series of contracts surrounding the contract-farming and the legislation that governs this group of contracts.

Moreover, on several occasions in this paper, we have raised the idea that a framework contract could allow this series of contracts to better meet the needs of the economic operation of the contract-farming, thereby allowing the judge and the parties to the contracts to have a coherent and effective framework. This will considerably help them to better understand the legal relationship of the whole and the various and numerous laws that are applicable.

CONTRACT FARMING IN VIETNAM POLICY ISSUES AND CHALLENGES



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Presentation structure

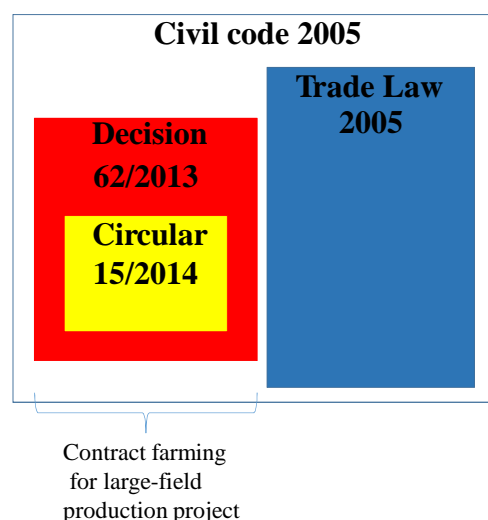
- Policy review of contract farming
- Comparison between Decision 80/2002 and Decision 62/2013
- Contribution of Decision 62 and Circular 15
- Impacts of Decision 62 and Circular 15
- Emerging issues of Decision 62 and Circular 15
- Conclusion

Policy review

Policy	Year	Issued by	Main content
Directive 100	1981	Communist Party	Introduction of output contract system between farmers and cooperatives (setting output quotas for households)
Ordinance 24-LCT-HDNN8	1989	National Committee	Guide of economic contracts between entrepreneurs
Decision 80/2002/QD-TTg	2002	Government	Promotion of contracting between entrepreneurs and producers in agricultural production with the facilitation of government and researcher (Four party policy)
Decision 77/2002/QD-BNN	2002	Ministry of Agri Rur Dev	Introduction of farming contract forms
Circular 05/2002/TT-NHNN	2002	Central Bank	Guide of providing loans in contract farming for related parties
Circular 04/2003/TT-BTC	2003	Ministry of Finance	Guide of financial issues when making farming contracts
Official Letter 886/HTPT-TDDP	2003	Vietnam Dev Sup Fund	Guide of providing loans in contract farming for related partners
Civil Code	2005	National Assembly	Reference for the general contracts
Trade Law	2005	National Assembly	Regulations on purchase and sale of goods
Decision 62/2013/QD-TTg	2013	Government	Promotion of production-processing-marketing linkages in large-field farming projects
Circular 15/2014/TT-BNN	2014	Ministry of Agri Rur Dev	Introduction of large-field farming concept and designing

Current policy framework of contract farming in Vietnam

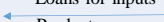
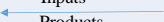
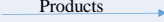
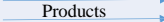
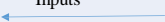
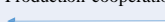
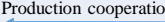
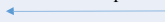
Policy	Main content
Civil Code	General contracts (types, obligations, breach, remedies)
Trade Law	Contracts on purchase and sale of goods between entrepreneurs and other parties (types, obligations, breach, remedies)
Decision 62/2013	Contracts in agriculture (subject, types, supports, breach) for large-field production projects
Circular 15/2014	Subjects, forms of agricultural contract, criteria of large-field farming



Context of Decision 62/2013 and Circular 15/2014

- Decision 80/2002 is largely considered as an unsuccessful policy (ADB 2005). In 2010, only 2.1% of rice, 13% fisheries, 0.9% vegetables and fruits, 2.5% coffee, 9% tea production were traded between smallholders and entrepreneurs under contracts (IPSARD 2012).
- Pilot models of large-field rice production in Mekong River Delta in 2011 and 2012 provided promising results (Ngoc 2012).

Decision 80/2002 vs Decision 62/2013 (1)

Subject	Decision 80	Decision 62	Difference
Contractual parties	Producers, entrepreneurs in agricultural production	Farmers, representative organization of farmers, entrepreneur in large-field farming projects	Decision 62 has narrower subjects (only large-field farming projects)
Partnership types	<div> <div>Loans for inputs</div> <div>(i) F  E</div> <div>Products</div> </div> <div> <div>Inputs</div> <div>(ii) F  E</div> <div>Products</div> </div> <div> <div>Products</div> <div>(iii) F  E</div> </div> <div> <div>Land as share</div> <div>(iv) F  E</div> <div>Products</div> </div>	<div> <div>Inputs</div> <div>(i) F, FO  E</div> <div>Products</div> </div> <div> <div>Production cooperation</div> <div>(ii) F  E</div> </div> <div> <div>Production cooperation</div> <div>(iii) FO  E</div> </div> <div> <div>Production cooperation</div> <div>(iv) F  FO</div> </div>	Decision 62 has broader contract forms, encourage the farmer's collective action

Decision 80/2002 vs Decision 62/2013 (2)

Subject	Decision 80	Decision 62	Difference
Supportive policies	Gov provides supports: land, investment, credit, technology, market, trade promotion	<u>Land</u> : E, F exempted fee and rent for lands for processing factories, store houses, worker accommodation. <u>Export and trade promotion</u> : (E), (F) prioritised for export contracts and temporary storage programs of gov. <u>Land field planning and improvement</u> : (E) partial fin support for transport, irrigation, electrical systems. <u>Plant protection cost</u> : (F) 30% in 1 st year, 20% in 2 nd year. <u>Technical training cost</u> : (E) 50%, (OF) 50%, (F) 100% for 1 time. <u>Seed</u> : (F) 30% fin support for seed cost in the first crop <u>Storage</u> : (F) 100% fin support for storage in E for max 3 months	Decision 62 has more specific supportive policies for each in contract farming party
Condition for supports	None	(E): have direct contract with F or FO, have an input supply zone meeting 50% of its total demand, drying, storage, processing systems (FO): have direct contract with F (F): have commitment to produce and sell products in contract.	Decision 62 has more precise conditions
Contract enforcement	No clear penalty	Parties will be withdrawn supports and are not eligible for next year	Decision 62 is more precise

Main content of farming contract regulated in Circular 15/2014

- Obligation of farmer
 - ✓ Sell agricultural products to E (time, area, quantity, place, quality)
 - ✓ If farmer does not buy inputs from E, she has to buy inputs certified by authorities
 - ✓ Obey the production procedure required by E
 - ✓ Inform plantation calendar for E
 - ✓ Compensate E if breach the contract
- Obligation of entrepreneur
 - ✓ Provide inputs (names, area, quantity, price, quality)
 - ✓ Buy agricultural products of F
 - ✓ Compensate E if breach the contract

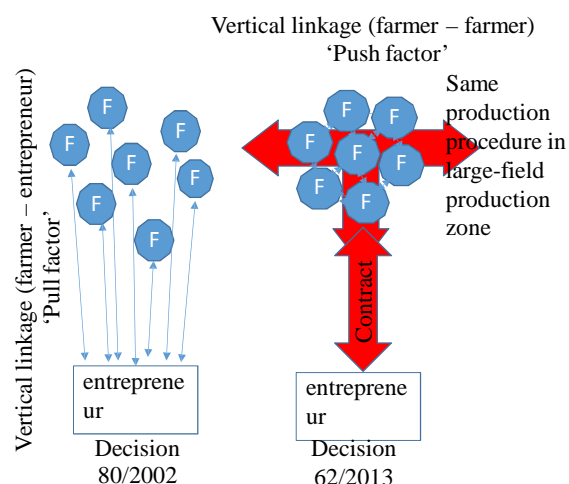
Criteria of large-field production zone regulated by Circular 15/2014

- Suitable with master plan of local authority
- Apply the same production procedure agreed by all parties
- One of the four linkage types
- Meeting requirements of local authority regarding land area (depending on local conditions)
- Appropriate pathway to establish production input zone

Crop type	Minimum % meeting the total demand for inputs of the entrepreneur						
	Year 1	Year 2	Year 3	Year 4	Year 5	Year 6	Year 7
Annual	10	20	30	40	50		
Perennial	10	15	20	25	30	40	50

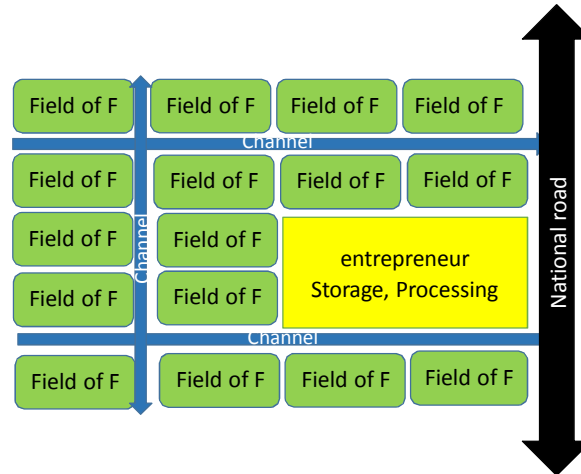
Rationale of Decision 62/2013 and Circular 15/2014 (1)

- Strengthen institutional linkage: Promote horizontal linkages between smallholders to promote the economy of scale for farmers
- Establish a better counterbalance between F and E, lead to better share: value, risk and decision power
- Create a focal points to receive supports of and provide feedbacks for government and researchers and



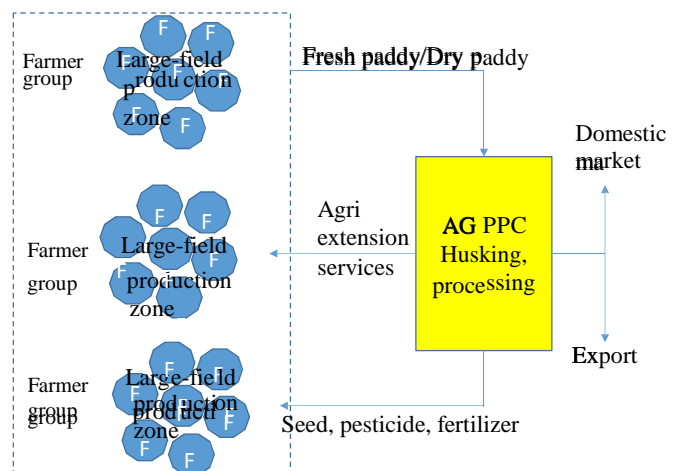
Rationale of Decision 62/2013 and Circular 15/2014 (2)

- Strengthen spatial linkage: Establishment of large-field production zone reduce transaction costs (transport cost, number of actor in the value chain, training, supervision...), increase the value added for F and E.



A successful example of Decision 62/2013 An Giang plantation protection company

- Rice production area: 2012 19,500 ha (6,500 smallholders), 2013 61,600ha (20,500 smallholders)
- Export: 2013, 300 tons to Japan (closed since 2008 due to high pesticide residue of VN)
- 4 factories (380,000 tons)
- Sell stocks for 6,000 smallholders
- Economic profits: smallholders who have contracts with AGPPC have \$US550 higher than others (Nghia 2012)



Source: Nghia (2012)

Impacts of Decision 62/2013

- In 2014, 11/13 provinces in Mekong River Delta implement contract farming with 134,000 ha, accounting for 10% total rice production (Custom Newspaper 2014).
- However, contract breach is still common. For example, in 2013, in Dong Thap province, Docimexco stock company breached the contract with farmers in total rice area of 1300 ha. Reason is both parties do not agree about the quality and price of rice. The company bought rice with lower price than market price by 200-300 VND/kg (People Newspaper 2014).

Emerging issues of Decision 62/2013 (1)

- Strict criteria of large-field production zone, requirements of E regarding infrastructure (big investment but is utilized in a short period) prevent E from engaging in large-field production.
- The same production procedure for the whole large-field in a contract is not well-defined → the contract enforcement is weak even though regulations on penalty for contract breach are available in Civil Code 2005 and Trade Law 2005.
- Market price fluctuations at harvest time → high price: farmers break contract and low price: entrepreneur breaks contract (Nhan and Takeuchi 2012)

Emerging issues of Decision 62/2013 (2)

- High risks of agriculture (price fluctuations, weather, disaster, pest, policy) cause high probability of contract breach from both F and E, but the high transaction cost for pursuing legal cases if conflicts happen and they do not have a habit to take legal cases (Nhan and Takeuchi 2012). Until now, there has been no legal cases happen between F and E about contract breach.
- Low transaction cost of contract breaching due lack of strict penalty, and easy to find substitute partners (low requirements on quality and safety) (Nhan and Takeuchi 2012)
- Contracts between smallholders and entrepreneurs who are not eligible for or do not participate in large-field production zones are not encouraged/abandoned? Most smallholders have small land areas (>87% smallholders have < 2 ha)

Conclusion

- Contract farming has been promoted recently in Vietnam but its impacts are still controversial and number of contract breach is still high.
- Policy recommendations:
 - ✓ For regions which have relative advantages in certain agri-products, designate and zone stable large-field production zones with intensive supports of government (technology, investment, loans...) for such products;
 - ✓ Promote the horizontal linkage between farmers and vertical linkage between farmer and entrepreneur by consolidate common procedure of production, processing and marketing;
 - ✓ Provide training for farmers and entrepreneurs about legal issues regarding contract farming;
 - ✓ Apply flexible price determination system, government supports market information, entrepreneurs improve their forecasting on market
 - ✓ Strengthen regulations on product quality and safety to create pressure on farmers and entrepreneurs
 - ✓ Establish mediation institutions/organizations to witness contract negotiation process and resolve farming contracts issues;
 - ✓ Promote the establishment of farmer's collective organizations;
 - ✓ Design policies to support contract farming activities for farmers and entrepreneurs who are not eligible for or do not participate in large-field production zones

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Long period of time to pursue legal cases

- According to Civil Code 2005, if there is a dispute, since the plaintiff send the complaint letter to the court, it takes about 4 months for the judgement for the first case . The period for appeal is 15-30 days. If there is appeal for the decision, it takes 2 months for the judgement for second case (review). After that, the winner has to send to the court the letter asking for the implementation of the judgement. It take from 3-5 months, even 1 year for the letter to be approved. Then, the loser has 30 days to voluntarily comply. Thus, the average period from sending the first complaint letter to the implantation of the judgement is from 1.5 to 2 years

Contract farming in Vietnam – Policy review and emerging issues

Khoi Dang¹, Dat Tran² and Dung Vu³

1. Introduction

Promoting contract farming practices is one of the main focuses of the Vietnamese government recently. Decision 889/2013/QĐ-TTg about *Restructuring agriculture towards enhancing value addition and sustainable development of the sector* considers contract farming as a pillar to implement this restructuring process. To promote contract farming practices, Decision 62/2013/QĐ-TTg (Decision 62) provides a number of regulations and supportive policies to encourage farmers and entrepreneurs to participate in agricultural contracts.

However, there are few studies which provide deep analyses regarding contract farming policy. Most studies so far have fallen into three categories: reviewing pilot contract farming models in practices (for example, ADB 2005; Nghia 2013), assessing the economic impacts of contract farming (for example, Costales et al. 2006; Tiongco et al. 2008; Saenger et al. 2013; and Saenger et al. 2014) and discussing reasons for contract breach (Nhan & Takeuchi 2012; and Trung 2008). We only found one paper (Trang 2013) providing a brief description about the main policies but it merely lists the main contents of current policies without any profound analysis. It can be seen that there is a lack of complete contract farming policy overviews which cover main policies in Vietnam over time.

This paper aims to address this literature gap by providing (i) a complete overview of contract farming policies over time, (ii) an analytical comparison between the two main contract farming policies: Decision 80/2003/QĐ-TTg (Decision 80) and Decision 62, (iii) a brief discussion about emerging issues related to Decision 62, and (iv) some policy recommendations.

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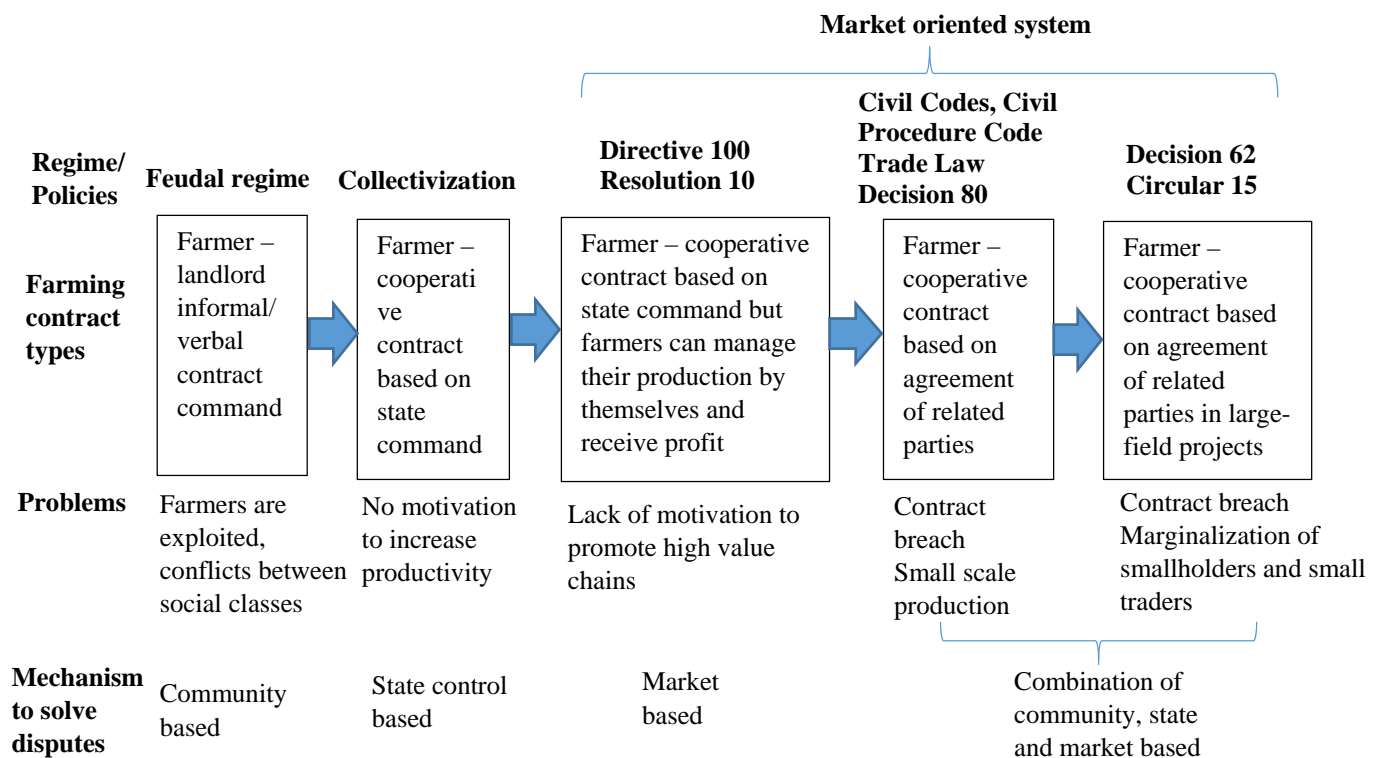
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2. Review of contract farming and related policies in Vietnam

Contract farming has been applied for a long period of time in Vietnam. In the feudal regime between 11th to 19th centuries, farming contracts were established between farmers who had no land and landlords who are abundant in land. Contracts might be made via signed documents or verbal agreement in which farmers had right to produce in the land of landlord and had to pay a large amount of their products to landlord as the land rent. In this contract system, farmers usually did not have negotiation power and were seriously exploited. This unfair production contract system has been maintained until the French colonial regime and created severe social inequality. This contract system came to an end when Vietnam claimed its dependence and reclaimed the land of landlords and allocated to farmers in 1956 (Son 2001).

From 1963 to 1980, Vietnam promoted its collectivization process in agriculture with the aim at establishing the paramount role of state-owned farms and cooperatives in controlling the sector. The Vietnamese Communist Party and the Government considered compulsory contract farming between farmers and cooperative management boards as the fundamental agricultural production form of the nation. In this contract regime, farming households had to contribute all their land to commune-level agricultural cooperatives and became cooperative members. All production activities of households were planned precisely by cooperative management boards. Cooperative leaders assigned the detailed tasks for and monitor the performance of their all members based on a marking system. At harvest times, each member would receive their awards (such as rice, meat, and other agricultural products) according to the evaluation of the cooperative management board. In this quasi-farming contract system, farmers cannot negotiate any contract terms (particularly the marking system and the reward mechanism) with their cooperative leaders. Instead, the level of production target and the marking system were decided by cooperative leaders under the direction of local authorities. The exclusion of farmers in the decision process of this contract system discouraged farmers to improve their productivity as most agricultural products of farmers were reclaimed by their cooperative management boards without fair compensations. Consequently, during 1970-1980, Vietnam's agriculture was in deep crisis due to extremely low productivity. Every year, Vietnam had to receive 1.6 million tons of food in the form of emergency aid from the communist alliance. Aquaculture reduced from 607 thousand tons in 1976 to 389 thousand tons in 1980 (Son 2001). The frustration of a large part of farmers increased and in many places farmers abandoned fields. (Cuc & Tiem 1996).

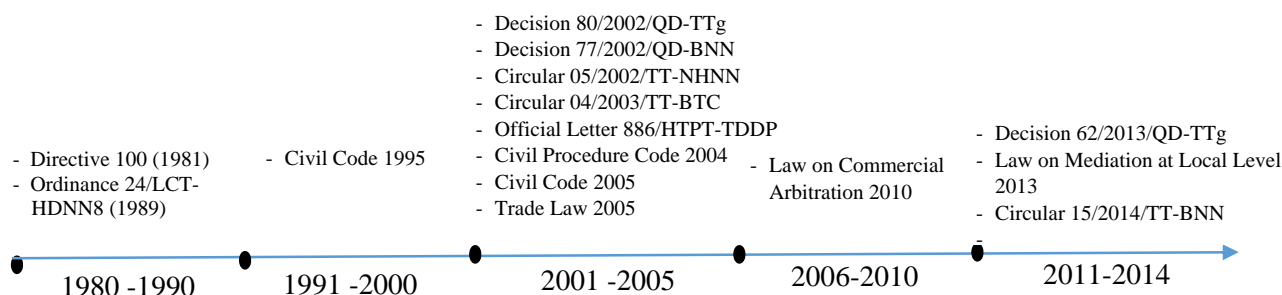
Figure 1. Evolution of contract farming practices over time in Vietnam



Source: Created by authors (2014).

In this context, revising irrational contract farming system was vital to Vietnam. Directive 100 CT/TW about ‘*improving contract mechanism, extending agricultural product contract with groups of farmers and individual farmers in agricultural cooperative*’ and Resolution 10/NQ-TW about ‘*reforming the management of agricultural economics*’ in 1988 was issued by the Party to encourage farmers to improve their productivity. In this framework, cooperatives allocated land for farmers in a fixed term and set the output quota that each household member has to fulfil. Instead of monitoring all production activities of farmers, cooperatives only provided seed, technical advices, fertilizer, pesticide and irrigation service. Farmers can keep, consume or sell to market all the amount above the required quota. Essentially, these policies replaced the marking system of farmer’s production performance by a quasi-market mechanism (i.e., these policies allowed farmers to enjoy higher reward/income when they increase their productivity).

Figure 2. Timeline of policies related to contract farming in Vietnam



Source: Created by authors (2014).

Box 1. Main content of Resolution 10

- Allow cooperatives to allocate agricultural land to farmers up to 15 years;
- Allow cooperatives to allocate important production inputs to farmers, such as buffalo, cattle and machinery equipment;
- Farmers can manage production procedure by themselves;
- Cooperatives provide services based on their member's demands;
- Apart from expenditure for cooperatives' services and taxes, farmers are allowed to use and sell their products in the market; and
- Trading relations between cooperatives and other actors are fair.

Source: Son (2001).

These two policies combining with a series of other policies in land management and trade liberalization, have significantly improved the agricultural productivity of Vietnamese farmers. During 1981-1985, although investment and input subsidy from the government reduced by 41.6 per cent and 58 per cent compared to those of 1976 -1980 period, rice production still increased by 27 per cent and the food import quantity declined by 4.6 million tons (Bich & Quang 1996). From 1988 to 1991, the total rice production area increased by 10 per cent from 5.7 to 6.3 million ha, and the rice production increased from 17 to 19.6 million tons. In 1989, Vietnam managed to export 1.4 million tons of rice for the first time (Son 2001). Since then, Vietnam has maintained to be one of the biggest agricultural exporting countries in the world.

The fact that the national agriculture has gradually become market oriented raised the need of consolidating the contract farming system to help protect better the benefits of related parties. During the 1990-2005, the legal framework⁴ governing contract farming has been gradually

⁴ Readers are referred to Trang (2013) for detailed description of Civil Code 2005, Trade Law 2005.

established with a number of laws, including Civil Procedure Code 2004, Civil Code 1995 (replaced by Civil Code 2005), Trade Law 2005, Law on Arbitration 2010, and Law on Mediation at Local Level 2013. Civil Codes 1995 and 2005 establish a general reference for all civil contract types and one may find several contract types relevant for contract farming including contract for property sale and purchase, contract for services, and contract for processing. General contents of a contract such as object, obligations and rights of related parties, risk management and termination of contracts are regulated in this document. Contract farming can also in the form of trade contracts which are governed by the Trade Law 2005 if (i) one party participating in contracts is a trader and (ii) contracted activities aim at generating profits including sale and purchase, service provision, investment and marketing. If disputes between contract parties occur, they can mediate or institute civil proceedings based on procedures regulated in Trade Law 2005, Civil Procedure Code 2004, Law on Arbitration Code 2010, and Law on Mediation at Local Level 2013.

Apart from legal documents, the Government also issues some specific regulations related to contract farming activities in the agricultural sector. In 2002, Decision No.80/2002/QD-CP⁵ (Decision 80) was issued by the Prime Minister on '*policies to promote selling agricultural products via contracts*' with the aim at accelerating agricultural transformation from subsistence to a commercialized and export-oriented agriculture. This is the first government's document which provides specific regulations on contract farming including contract forms, supportive policies for contract parties (farmers and entrepreneurs), and remedies in events of conflicts. Apart from those, this decision also encourages the involvement of local governments and related ministries and research institutions to improve contract efficiency, and to promote technological innovation in the rural economy. Thanks to this policy, in Vietnam during 2002-2012, four types ⁶of agricultural contracts including multipartite, centralized, nucleus estate, and informal/verbal have been established (ADB 2005). Some agricultural commodities witnessed high rates (more than 80 per cent) of contracts such as sugar, milk, cotton and tea (MARD 2008). Nevertheless, this policy has been largely recognized as an unsuccessful policy (ADB 2005, ADB 2006). In 2010, only 2.1 per cent of rice, 13 per cent of fisheries, 0.9 per cent of vegetables and fruits, 2.5 of coffee, 9 per cent of tea production were traded between smallholders and entrepreneurs under formal

⁵ Readers are referred to Trang (2013) for detailed description of Decision 80/2002/QD-CP.

⁶ Readers are referred to ADB (2005) for detailed explanations of each contract type.

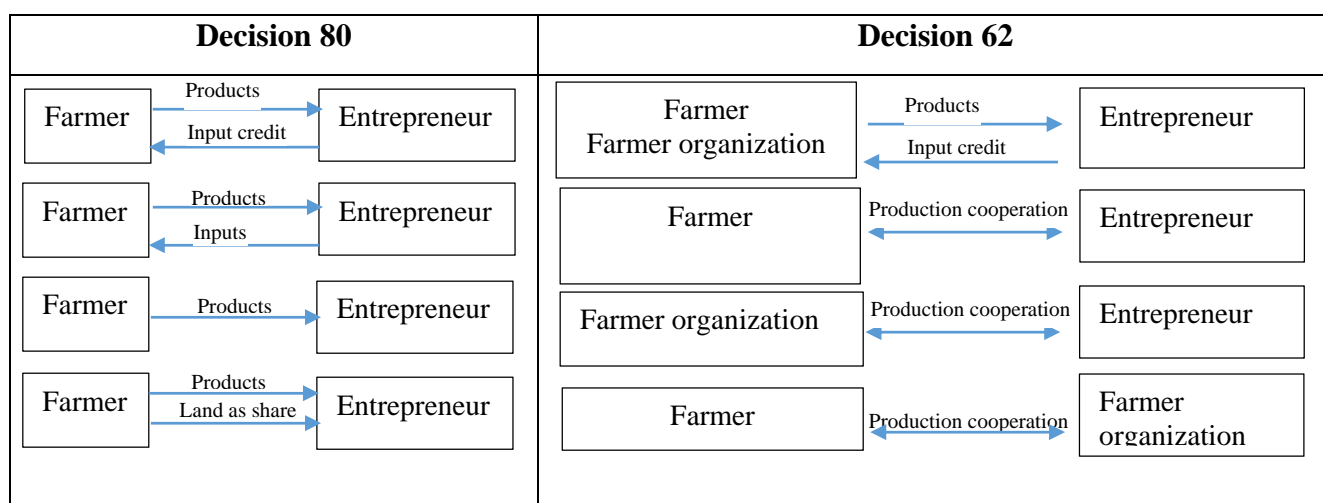
contracts (IPSARD 2013). Moreover, there were a great deal of number of contract breach cases in this period (MARD 2008; Nhan & Takeuchi 2012).

To address this issue, most recently, Decision 62/2013/QD-TTg (Decision 62), was issued by the Prime Minister replacing Decision 80, with the aim at '*promoting the development of contract farming between enterprises, representative organization of farmers and individual farmers in agricultural projects in large-field production zones*'. This decision clearly prescribes (i) four types of contract-based cooperation which are eligible for supports and (ii) a number of supportive policies that parties of contract farming may enjoy. To facilitate the implementation of this Decision, the MARD issued Circular 15/2014/TT-BNNPTNT to introduce a standard contract form which can be used in contract-based cooperation activities regulated in Decision 62.

3. Comparison of Decision 80 and Decision 62

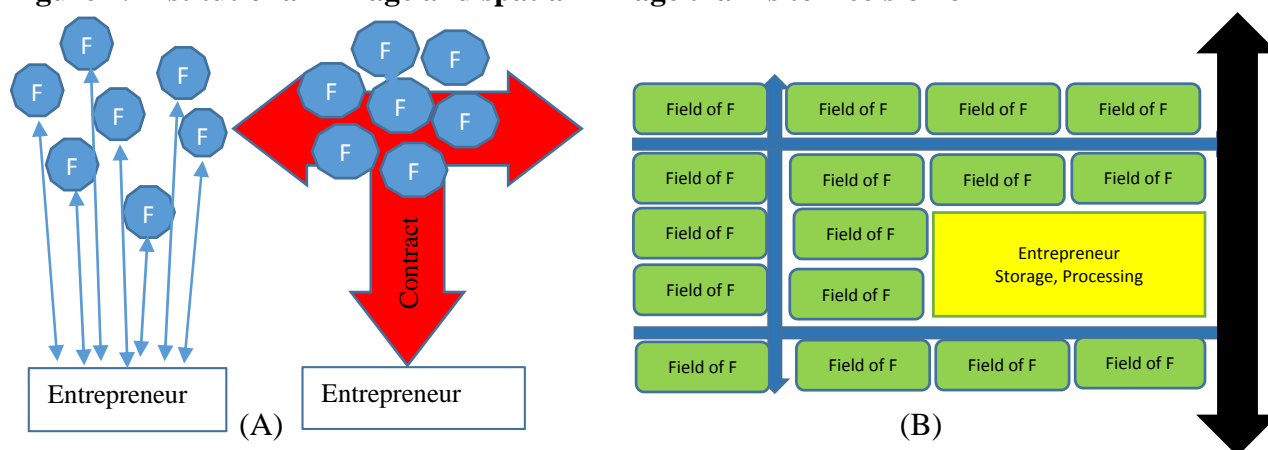
Based on the background of the previous section, this section attempts to analyse how advantageous Decision 62 over Decision 80 based on several categories. First, compared to Decision 80, Decision 62 regulates broader scope of contract parties and contract forms. While the former only regulates the contractual relationship between individual farmers and entrepreneurs, the latter allows agricultural contracts between individual farmers as well as representative organizations of farmers with entrepreneurs (Figure 3). Moreover, different to Decision 80 which covers all agricultural activities, Decision 62 only focuses on large-scale agricultural projects. These two differences mean that Decision 62 encourages farmers to promote horizontal cooperation between farmers (institutional linkage in Figure 4A) and merge small land plots into large zones (spatial linkage in Figure 4B) take advantage the 'economies of scale' effect. The two linkages will help reduce transaction costs of both contract parties (farmers and entrepreneurs) including reduction in number of stakeholders in the value chain and the cost of transport, training, collection, and monitoring (Nghia 2012). In addition, these linkages also improve the power balance between the two contract parties which might help allocate value, risk, and decisions in a way that is mutually beneficial, ideally sharing risk, and improving quality and production (Ngoc 2012). This will increase the likelihood of successful contracts as suggested by Sykuta and Parcell (2002). Strengthened linkages also enable farmer's organizations to become focal points to receive supports of and provide feedbacks for interventions of government and researchers as the successful case of An Giang Plant Protection Stock Company (Nghia 2012).

Figure 3. Summary of contract forms in Decision 80 and Decision 62



Source: Created by authors (2014).

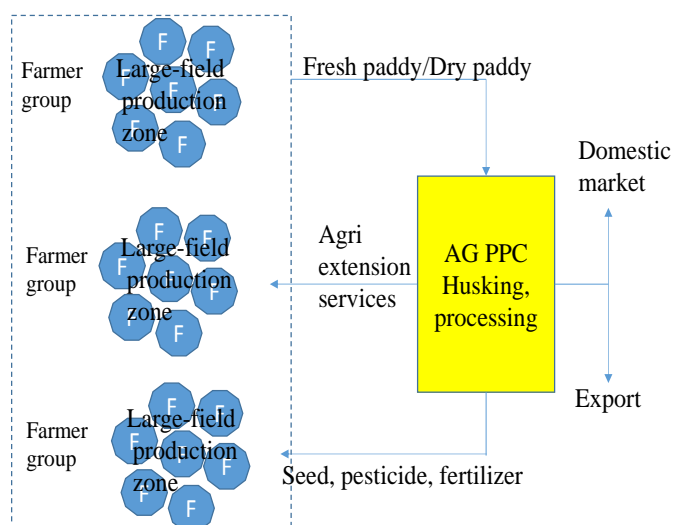
Figure 4. Institutional linkage and spatial linkage thanks to Decision 62



Source: Created by authors (2014).

Box 2. Successful case of An Giang Plant Protection Stock Company

- Rice production area: 2012 19,500 ha (6,500 smallholders), 2013 61,600ha (20,500 smallholders)
- Export: 2013, 300 tons to Japan (closed since 2008 due to high pesticide residue of VN)
- 4 factories (380,000 tons)
- Sell stocks for 6,000 smallholders
- Economic profits: smallholders who have contracts with AGPPC have \$US550 higher than others



Source: Nghia (2012)

Second, regarding supportive policies and conditions for supports, while Decision 80 has merely generic supports for contract parties regarding land, investment, credit, technology, market, and trade promotion, Decision 62 elaborates detailed supportive policies (Table 1). These detailed regulations would help contract parties gain better access to the government's supports in reality and promote contract farming more rapidly. In addition, the new decision also has strict conditions that farmers and entrepreneurs have to obey if they desire to receive the supports of the policy. Two main conditions include: (i) parties have contract, (ii) they obey the contract commitments. Moreover, for entrepreneurs, they are required to have their own material supply zone.

Table 1. Summary of supportive policy of Decision 62

Types of support	Amount
Land	Entrepreneurs, famers are exempted from fee and rent for lands for processing factories, store houses, worker accommodation
Export and trade promotion	Entrepreneurs, famers are prioritised for export contracts and temporary storage programs of the government
Land field planning and improvement	Entrepreneurs receive partial financial supports for transport, irrigation, electrical systems.
Plant protection cost	Farmers receive supports for 30% total cost in 1 st year, 20% total cost in 2 nd year.
Technical training cost	Entrepreneurs receive support 50% for technical training cost, farmer organization: 50%, farmers: 100% for one time
Seed	Farmers receive 30% financial support for seed cost in the first crop
Storage	Farmers receive 100% financial support for storage in entrepreneurs for maximum 3 months

Source: Created by authors (2014).

4. Discussion

Remaining issues

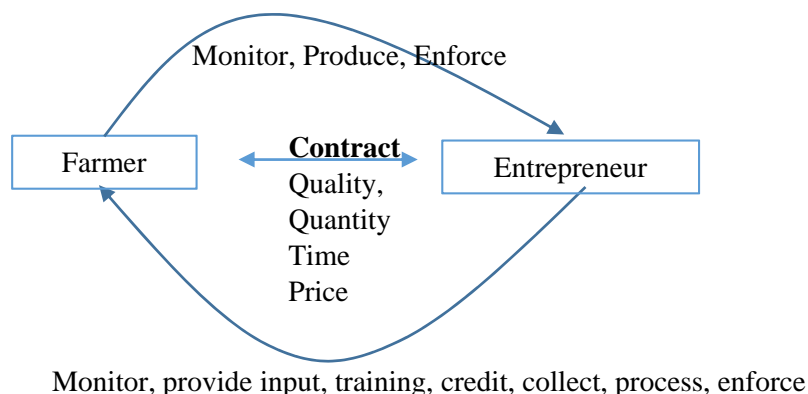
Lack of a contract enforcement mechanism to mediate disputes

One of the biggest problems regarding contract farming in Vietnam is that farmers and entrepreneurs usually breach their contract in harvest time, when market price fluctuates (Trung, n.d). Theoretically, at any point in time during a contract, both parties assess the costs and benefits of breaking their deal, i.e., when the benefits of breaking the contract are greater than the capital and reputation losses for one party, this party will breach the contract; otherwise, they will respect it (Gow et al. 2000; Prowse 2012). In Vietnam, the main difficulty is that when the price fluctuates, the cost of obeying the contract is often higher than that of breaching the contract (Nhan & Takeuchi 2012; Trung n.d). If disputes happen,

pursuing legal cases will outlay both time (Box 2) and wealth (e.g., legal procedure cost accounts 30 per cent contract value) of parties (Trung n.d). In contrast, the cost of contract breach is almost nothing due to the lack of strict penalty, and the ease to find substitute partners due to low requirements on agricultural product quality and safety (Nhan & Takeuchi 2012).

Similar to Decision 80, Decision 62 fails to address the problem of contract breach as it neither reduce the cost encountered to resolve contract conflicts nor raise the cost of breaking contract's commitments of related parties. When entrepreneurs and farmers participate in a contract, transaction costs are incurred by both parties (Figure 5). Williamson (1979) identified two main forms: ex ante (such as the costs of finding a trading partner, negotiating terms, drafting, safeguarding and monitoring an agreement); and ex post (the costs incurred to settle a dispute, such as legal fees, as well as the spill-over costs into the firm's activities and pricing levels). By strengthening institutional and spatial linkages and providing financial supports, Decision 62 attempts to reduce all ex-ante costs related to production and marketing processes and to sustain long-term relationships between parties. This document, nevertheless, does not mitigate the ex-post costs related to the settlement of contract disputes as it regulates all contract conflicts are resolved by Civil Code 2005, Civil Procedure Code 2004 and Trade Law 2005 and has no guideline to simplify the process of contract's conflicts settlement. Moreover, Decision 62 does not raise the cost of contract breach. The penalty mechanism regulated by the Decision (withdrawing already provided supports and cut supports of the violated party in the following year) is not insufficiently powerful to increase the transaction cost of breaking contract.

Figure 5. Transaction costs of contract farming



Source: Created by authors (2014).

Box 3. Lengthy procedure to resolve conflicts in agricultural contracts***Based on courts***

According to Civil Procedure Code 2004, if there is a dispute which cannot be resolved by negotiation or mediation, the plaintiff will sue case into the court by a petition. It takes about 4 months for the judgement for the first instance. Then, if any parties does not satisfy to the judgment of the court, she/he may appeal to the Appeal Court. The period for appeal is 30-60 days. It takes additional 2 months for the judgement for Appeal Court. There is also another remaining special case under the Supreme Court which cannot predict the term and proceedings further. If everything is acceptable, the winner has to send to the Provincial Department of Civil Judgement Enforcement a letter asking for the implementation of the judgement. It take from 3-5 months, even 1 year for the letter to be approved. Then, the loser has 30 days to voluntarily comply. Thus, the average period from sending the first complaint letter to the implantation of the judgement is from 1.5 to 2 years.

Based on arbitration

In parallel with dispute resolution by courts, the disputes resolution by arbitration is also applicable in Vietnam. The legal system for arbitration activities has been quite fully set forth, and there is mechanism guaranteeing the execution of arbitration awards, thus increasing the effectiveness of dispute resolution by the arbitration. The arbitration body which is considered the most experienced and best recognized is Vietnam International Arbitration Centre (VIAC) in conjunction with the Vietnam Chamber of Commerce & Industry (VCCI).

The cases resolved by arbitration is, however, not common as with the cases settled by courts. This reality could be explained by both legal provisions and practices. Firstly, the arbitration institutions are established in Ho Chi Minh City and Hanoi only, while agricultural areas in Vietnam are mainly in other provinces. The lack of local arbitration institutions causes hersitation of the contracting parties, especially the farmers, to submit their cases to arbitration institutions. Secondly, arbitration's procedure in Vietnam has not yet been as simple as it should be in compare with the procedure at courts. It comes from the unspecific legal regulations on arbitration. The Law on Commercial Arbitration 2010 provides the time limit for notice obligations, submission of the defendant's defence, establishing arbitration council and electing of chairman of arbitration council. However, the LCA is not specified the time limit for issuing of arbitration decision from the time of establishing arbitration council. As there is no specified time limit as mentioned above, in fact, these cases are time-consuming. There are cases have lasted for more than 01 year to get the arbitration award. Under European Convention on International Commercial Arbitration, 09 months from the election of the arbitration chairman, the arbitration must issue the decision. This provision should be taken into account to be added into the LCA. Thirdly, different from the court, the expense for arbitration procedure is comparatively high with minimum of 2,500USD per case (VIAC's fee). The agricultural contracts in Vietnam are mostly in small and medium sizes, therefore, the high cost is also giving difficulties for contracting parties.

Source: Created by authors based on Civil Procedure Code 2004 and Law on Commercial Arbitration 2010.

Lack of contract form suitable to real-life condition

Another issue is the lack of suitable forms of agricultural contract in Decision 62. According to ADB (2006), to improve the enforcement of contracts, related parties should specify various detailed terms of trade (e.g. prices, quantities, delivery dates, payment terms), and input provision and production specifications (i.e. the use of particular production practices). To facilitate Decision 62's implementation, nevertheless, Circular 15/2014/TT-BNNPTNT only regulates one type of contract covering all type of agricultural services. This unique contract form is too generic and not useful as it does not address the potential "choke-points" in the coordination process between farmers and entrepreneurs that could compromise the use of contract. For example, Circular 15/2014/TT-BNNPTNT does not specify the concept and criteria of 'the common production procedure', which is the backbone for the contract in large-scale projects. Thus, the lack of details of contract forms may make the room for potential disputes in the future.

Emerging issues

Difficulty of entrepreneurs in meeting requirement of Decision 62

Although supportive policies are specified in Decision 62/2013/QD-TTg, it is not easy for entrepreneurs to access them in reality. Entrepreneurs who desire to access supportive policies and preferential credit conditions are required to qualify five conditions: (i) large-field project is suitable with master plan of local authority, (ii) apply the same production procedure agreed by all parties, (iii) are one of the four linkage types, (iv) meet requirements of local authority regarding land area (depending on local conditions), and (v) have an appropriate pathway to establish production input zone (Table 1). While the four former requirements are quite easy to be achieved, the fifth is a great challenge to entrepreneurs as this requires their huge investments including land consolidation (persuading and compensate for farmers to swap/exchange and merge their land plots to a big area), infrastructure establishment (processing machines, storage houses, etc). For example, to establish a large-field zone for rice production of 1000 ha in Mekong River Delta with two harvesting seasons per year, a firm has to invest about 2.5 million USD (Dat 2014). Thus, it is not easy to medium-size entrepreneurs (with the average revenue of 50,000 USD to 100,000 USD per year, Dat 2014) to participate in large-field production project, i.e., to be eligible to Decision 62, given the difficulty in accessing credit from banking system.

Table 2. Requirements of pathway to establish the large-field production zone

Crop type	Minimum % meeting the total demand for inputs of the entrepreneur						
	Year 1	Year 2	Year 3	Year 4	Year 5	Year 6	Year 7
Annual	10	20	30	40	50		
Perennial	10	15	20	25	30	40	50

Source: Circular 15/2014/TT-BNNPTNT.

Difficulty of smallholders in participating in large-field production zones

Assuming contract farming can improve the welfare of households, the relevant question is how the Vietnamese government can help agricultural entrepreneurs and smallholders who are not eligible to Decision 62 to participate in contract farming. As mentioned in Part 3, a key component for farmers to participate in large-scale projects as regulated in Decision 62 is bettering their organizations. However, even if the poor are engaged in production areas where contracts may help to add value, it is not clear whether the poor can be organized, or organize themselves, to link with other actors in the value chain to effectively use such types of mechanisms (ADB 2006). This suggests several areas that need further examination. Firstly, what types of organizational forms among producers could be employed to coordinate activities with other parties in the value chain through contracts? Second, how do these organizational forms vary by product? Third, can organizations be developed that are in the interests of those participating in them? And, forth, for households who cannot participate in such organizations, what policies that the government should be issued to help them.

5. Conclusion and recommendations

Contract farming is always a main pillar for the agricultural development throughout the history of Vietnam. Contract farming and related policies in Vietnam has been witnessed an upward spiral evolution. Beginning from an unfair system in feudal regime, contract farming has progressed to compulsory state-command contract system, to a loosely market oriented contract system and finally to a strict market oriented contract system. Apart from establishing a fundamental legal framework including Civil Code 2005, Civil Procedure Code 2004, Trade Law 2005, Law on Arbitration 2010, and Law on Mediation at Local Level, Vietnam also issues specific sectoral policies including Decision 80 and Decision 62 to promote the contracts between farmers and entrepreneurs. Nevertheless, these policies fail to strengthen the enforcement mechanism between related parties, to provide precise contract

forms for specific products, and to provide easy access to supportive policies for related parties.

Based on these issues, some policies are recommended including:

Improving the system of contract law in the agricultural sector is one of the key solutions contributing to the development of agricultural contract. As analysed above, the legal documents to handle relationships in contract farming in Vietnam is still lacking, incomplete and inconsistent. Some policy initiatives can be considered. First, legislators need to consider the creation of a new separate chapter in the Civil Code and Commercial Law adjusting agricultural contractual relationships. It is in need to state whether agricultural consumption contract is a civil contract or commercial contract. This regulation shall play an important role to state the source of law to adjust contract. In addition, the laws also need to adjust the specific the ownership of agricultural products in the case of mutual investment, as in this case, agricultural production are common property of farmers and businesses. Another solution may be the issuance of a decree on contract for trading agricultural products. This decree must be clarified five modes of agricultural consumption contracts, which are: centralized mode, nuclear farm mode, multi-entity mode, informal mode and intermediate mode (Trung, 2009). It is necessary to determine the rights and obligations of the participants in the contract under each mode. Legislators should issue specific contract templates for each form. In each type of contract should specify each party's responsibility for technical, financial aspects, management and valuation methods. In the long run, an Agricultural Law which contains a chapter relating to the agricultural contracts may also be built.

Improving legal system relating to agricultural land is also important. Based on experience in many countries around the world, as well as the practical agricultural contract in Vietnam, only farms producing a large scale productions can be performed as well as are in need to be performed under a contract farming. Therefore, Vietnamese Government should adjust and improve the land accumulation policy for the development of agricultural farms producing large-scale commodities. To improve accumulating land policy, the provisions relating to quotas for acquisition of agricultural land should be abolished. The Land Law 2013 and the Resolution of the National Assembly Standing Committee No.1126/2007/NQ-UBTVQH11 dated 21 June 2007 set up a strict legal provisions on allocation quotas for agricultural land and quota for acquisition of agricultural land use rights by households and individuals. These regulations, however, cause much difficult for individuals and institutions to expand their

scale of production. Moreover, the government should designate stable large-field production zones with intensive supports of government in regions which have relative advantages in certain agricultural products. The model of An Giang Plant Protection Stock Company in rice production could be a good example for this type of policy.

In terms of resolving contract disputes, it is vital to reduce the transaction cost of related parties who obey contracts and increase the transaction cost of the ones who breach contracts. Several policies can be considered to apply:

- Simplify legal procedures for resolving contract disputes in courts and by arbitration;
- Consolidate local level mediation institution and establish third-party mediation institutions to witness contract negotiation process and resolve farming contracts issues. Some studies show that both farmers and entrepreneurs can improve their contract efficiency in dairy industry in Vietnam in the case of Vinamilk company (Saenger 2013; Saenger 2014);
- Provide training for farmers and entrepreneurs about legal issues regarding contract farming;
- Supports market information for smallholders who participating agricultural contracts;
- Strengthen regulations on product quality and safety to create pressure on farmers and entrepreneurs. Trung (n.d) argues that stricter quality and food safety standards may reduce the chance of contract breach as both farmers and entrepreneurs are hard to find the substitute products outside;

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APPENDIX 1. SUMMARY OF MAIN POLICIES RELATED TO CONTRACT FARMING IN VIETNAM

Policy	Year	Issued by	Main content
Directive 100	1981	Communist Party	Introduction of output contract system between farmers and cooperatives (setting output quotas for households)
Ordinance 24-LCT-HDNN8	1989	National Committee	Guide of economic contracts between entrepreneurs
Civil Code	1995	National Assembly	Reference for the general contracts
Decision 80/2002/QD-TTg	2002	Government	Promotion of contracting between entrepreneurs and producers in agricultural production with the facilitation of government and researcher (Four party policy)
Decision 77/2002/QD-BNN	2002	Ministry of Agricultural and Rural Development	Introduction of farming contract forms
Circular 05/2002/TT-NHNN	2002	State Bank	Guide of providing loans in contract farming for related parties
Circular 04/2003/TT-BTC	2003	Ministry of Finance	Guide of financial issues when making farming contracts
Official Letter 886/HTPT-TDDP	2003	Vietnam Development Supporting Fund	Guide of providing loans in contract farming for related partners
Civil Procedure Code	2004	National Assembly	Guide of resolving contract disputes
Civil Code	2005	National Assembly	Reference for the general contracts
Trade Law	2005	National Assembly	Regulations on purchase and sale of goods
Law on Commercial Arbitration	2010	National Assembly	Regulations on arbitration of disputes in commercial contracts
Decision 62/2013/QD-TTg	2013	Government	Promotion of production-processing-marketing linkages in large-field farming projects

Law on Mediation at Local Level	2013	National Assembly	Procedure of mediation for contract breach at local levels
Circular 15/2014/TT-BNN	2014	Ministry of Agricultural and Rural Development	Introduction of large-field farming concept and designing

Source: Collected by author (2014).

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Supreme National Economic Council (SNEC)

Promoting Good Contract Practices between Producers and Buyers in Contract Farming
Operation in the Asia Context

WORKSHOP ON THE LEGAL DIMENSION OF CONTRACT FARMING

Presentation on Practical Experiences on Contract Farming Formation and Obligation of the Parties

26th September 2014

CONTENT

1. Contract Farming Situation in Cambodia
2. Format of CF
3. Key stages in facilitating a Contract Farming Process
4. Duties and rights of both parties
5. Contract formulation
6. Upcoming challenges

1. Contract Farming Situation in Cambodia

- ❖ Royal sub-decree 36 on Contract Farming (promulgated Feb, 2011):
 - Strengthening the responsibility and trust between producing and purchasing parties base upon the principles of equality and justice.
 - Ensuring the accuracy of the prices, purchases, and supply of agricultural products, both quantity and quality
 - Increase purchasing, processing and exporting of agricultural products
 - Contribute to national economic development and people's poverty reduction pursuant of the policies of the Royal Government

1. Contract Farming Situation in Cambodia (Con't)

- ❖ Component #3 of SCCRP project (Promoting Contract Farming and Enhancement of Roles of Farmer Organizations in Paddy Collection and Processing)
 - Finalization and improvement of the legal framework on CF
 - ✓ Study on practices of CF in Cambodia
 - ✓ Test PIAs on CF
 - ✓ Creation of Coordination Taskforce on CF (Organize 1st meeting of CBAP committee, organize the workshop with stakeholders, draft formal contract and guideline of CF ...etc.)
 - ✓ ...etc.

2. Format of CF

There would be 12 articles in the format of CF:

1. Object
2. Duration
3. Rights and duties of the PRODUCER
4. Rights and duties of the BUYER
5. Harvest and transportation
6. Determination of product quality
7. Price
8. Payment
9. Disasters
10. Termination of contract
11. Conflict resolution
12. Development of the contract and language



3. Key stages in facilitating contract farming process



4. Rights and duties of both parties

PRODUCER

- To comply with conditions as inscribed in the agreement
- To proceed production activities based on seasonal and required timeframe
- To supply on time, in term of grade, quantity, and quality and due timeline
- To Access the payment of product value as set in agreement

BUYER

- To comply with conditions as inscribed in the agreement
- To determine the commodity items such as quantity, quality, place, and date of delivery and acceptance of the commodities
- To provide agricultural materials such as vegetable or crop seeds, animal breeds, and provide credit advance, technical services ...etc.
- To pay by specific unit – based products and quality as agreed prices
- To pay the commodities to producing party as specifying under the conditions and at specific timeframe as agreed upon.

5. Contract formulation

1. Object:

- Objective of the contract?
- Quantity of product(s) to be supplied and bought?
- Attachment of list of farmers/producers?



2. Duration: exact duration of the contract (starting date and finish of the contract)

3. Rights and duties of the PRODUCER:

- Which varieties? Total land size?
- Quantity of product(s) to be supplied and linked to the quality needed?
- Receive financial and technical support from the BUYER
- Mobilize members to participate in the training(s)
- Complaint during implementation of the contract about the failure of any commitment of the BUYER
- Shall be responsible before the law or provide the compensation for the loss in case it does not fulfill the commitments within a liability limitation in cash equalled an amount assessed the failure of the commitment ...etc.



5. Contract formulation (Con't)

4. Rights and duties of the BUYER

- Commitment to buy the product(s) in compliance with agreed quantity and price
- Provide supports to PRODUCER (Financial or technical supports)
- Provide bonus to involved FO(s)
- Provide the payment in advance to buy the product(s)
- Shall be responsible before the law or provide the compensation for the loss in case it does not fulfill the commitments within a liability limitation in cash equaled an amount assessed the failure of the commitment ...etc.



5. Contract formulation (Con't)

5. Harvest and transportation

- Agreement on the harvesting time between both parties
- Collection point
- Time of product(s) delivery
- Agreement in case of late transportation
- ...etc.



6. Determination of product quality

- How to check the quality?
- Specification of product(s) (moisture, color, foreign matters, smell, purity ...etc.) ? 1st quality? 2nd quality?



7. Price:

- How to determine the price? it depends on the quality?
- Agreed price (based on market price? if yes, when?) ...etc.

5. Contract formulation (Con't)

8. Payment

- Delivery of product(s) and payment time
- Proof of payment
- How to pay? by cash? by bank transfer? if by bank transfer, account of individual farmer? Or account of Farmer Organization?
- Who will be in charge to pay for the bank transfer?
- ...etc.



9. Risk of natural disaster

- Kind of disasters (heavy flood, drought, fire, pest ...etc.)
- Time to inform the BUYER
- Who will evaluate the disaster to be agreed by both parties
- Automatic cancellation of the contract



5. Contract formulation (Con't)

10. Termination of contract

- Condition of the termination of contract
 - all commitments are fulfilled by both parties?
 - One party proposes to finish the contract?
 - ...etc.

11. Conflict resolution

- At Producer and Buyer Level
- At Provincial Department of Agriculture Level
- At National Level (through Contract-based Agricultural Production Committee: CBAPC)



12. Development of the contract and language

- Condition to make the contract (volunteer, no force ...etc.)
- Language of the contract
- Number of copies of the contract

➤ *Each party should find person to be witness. After signing the contract, it will be sent to DAI-MAFF for the endorsement.*



6. Upcoming challenges

To enforce pursue the development of Contract Farming:

- ❑ Contract-based Agricultural Production Committee (CBAPC) defined in the sub-decree is the national level. To ensure the regulation at local level, delegation should be given to provincial or district levels, and thresholds defined to determine the level that shall be mobilized (e.g. not refer to the Minister level issues regarding local contract with a value of few thousands US Dollars, for instance)
- ❑ Development and approval on official format of CF and guideline for facilitation and registration of contracts. Given limited resources of the Administration, its role might face limitations, and the involvement of non-governmental stakeholders could be seen as a support. Guidelines/formats shall also leave a large flexibility (guides on what shall be addressed by the contract, but not on how it shall be addressed: in other words guidelines shall be questions rather than answers.

6. Upcoming challenges (Con't)

- ❑ A major challenge is the need of a CULTURAL change in the Public Administration: a culture of service and cost efficiency shall emerge instead of a culture of control and imposition of heavy procedures.
- ❑ Develop support measures / incentives to encourage contract farming agreements WHEN IT CONTRIBUTES TO POLICY OBJECTIVES. Contract-farming is not an objective in itself but might be a tool.
- ❑ Develop arbitration procedures and enforcement of arbitration decision: signatories of the contract sign to be secured (in their market or in their supplies), but unless contracts can be enforced, contract farming cannot provide the expected level of security. An important challenge is to cover risks that are out of the control of both parties (climate or pest risks, notably): possible linkage with crop insurance development?

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Thanks for your attention!
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Designed the 8 step clustering approach to Agro-enterprise Development;

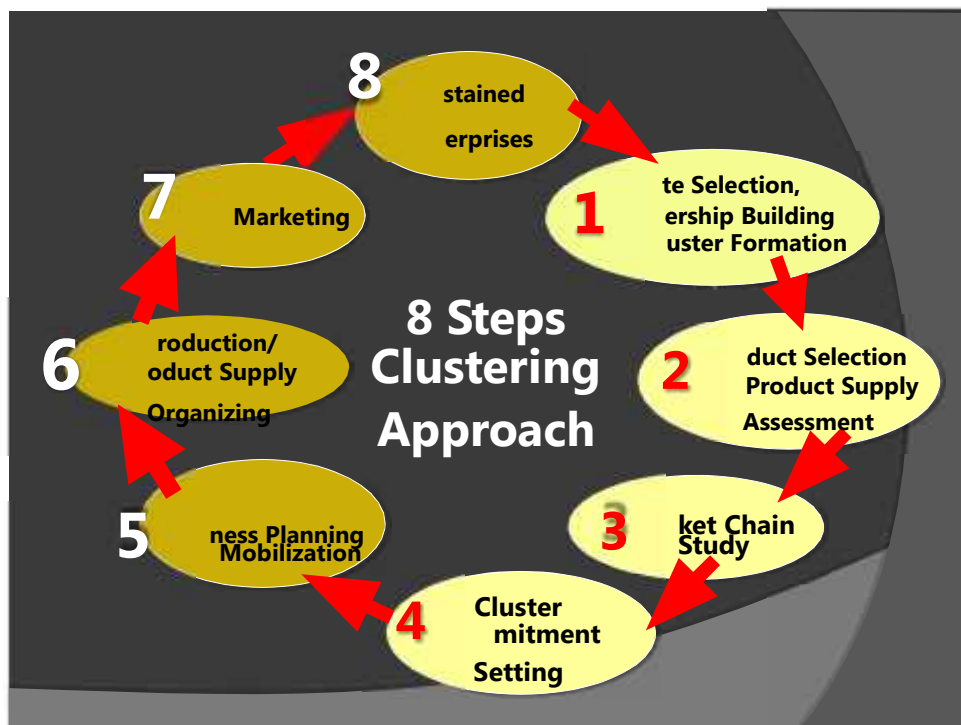
Provides technical assistance in the Farmer Entrepreneurship Program (FEP)

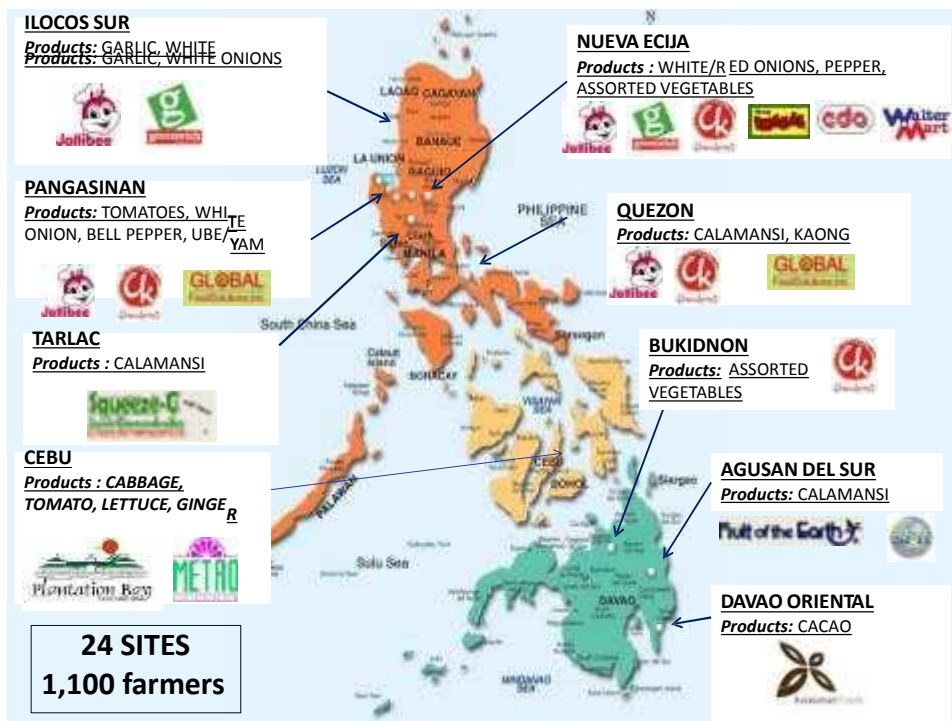
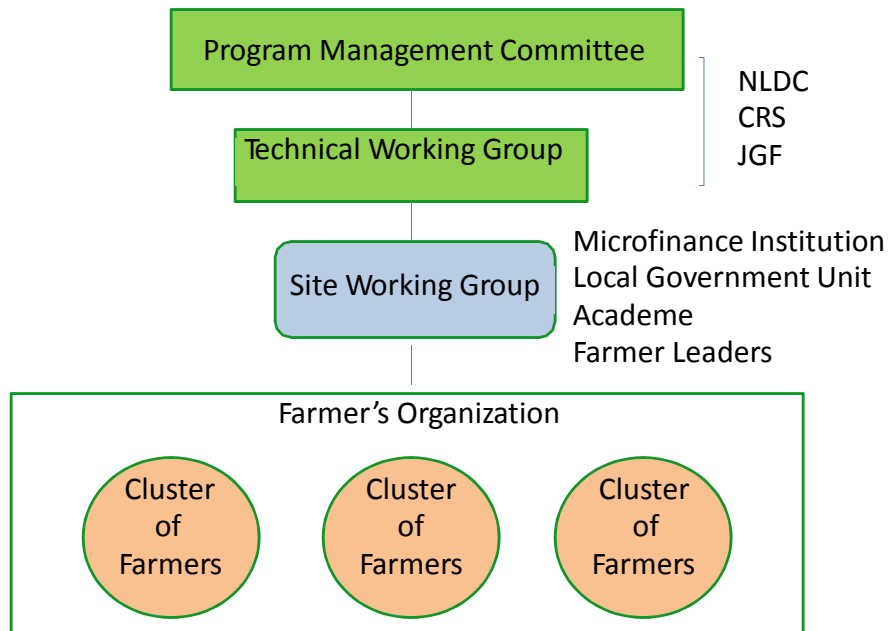


Partners

The Corporate Social Arm of the Jollibee Group Corporation, the biggest local food chain company in the Philippines;

Has assumed the role in FEP of helping find institutional markets for the farmer groups;





Legal Documents/ Marketing Agreements

- ❖ Supply Contract
- ❖ Purchase orders
- ❖ Delivery receipts
- ❖ Oral agreements
- ❖ Accreditation certificate
- ❖ Electronic Communication (portal, emails, SMS, etc.)
- ❖ Full disclosure statements from MFIs

Note: Marketing Agreements are between the institutional buyer and farmer group



Common Practices in FEP sites

- Contract is usually for 1-3 years;
- Reasonable clauses for renewal, non-compliance due to force majeure, breach of contract (e.g. non-compliance for x no. of times)
- Price is indicated and determined based on product quality / classification;



Common Practices in FEP sites

- In some cases, price renegotiation may be done after 3 months if variance with local price is too big;
- Technical assistance is sometimes provided by the buyer
- Hauling, post-harvest facilities are usually the responsibility of the farmer-producer



ISSUES AND CONCERNS

- Farmers are still generally not well-educated and uncomfortable with formal agreements
- Risk is basically mostly shared by the Microfinance Institution (MFI) and the farmer;
- Non-compliance is often caused by farmers not meeting required volume, quality due to production-related problems, natural calamities, force majeure, some sideselling



ISSUES AND CONCERNS

- Farmers have little or no control on the Buyer's product sorting/classification system which also affects price and overall sales and income
- Financing packages by MFIs are mostly limited to production loans. Value-chain based financing windows for hauling, processing, post-harvest equipment are needed to ensure consistent quality, mitigate risks and strengthen the agro-enterprise.



CONCLUSIONS AND FUTURE DIRECTION

- Continue capacity building interventions that enhance farmer's knowledge and skills on agro-enterprise management, governance and basic financial management;
- Legal/marketing agreements should be simple, clear, concise and preferably in the local dialect
- Importance of full transparency, fairness and viability should be emphasized and protected, particularly for the farmers.



CONCLUSIONS AND FUTURE DIRECTION

- Use of Agricultural Guarantee funds, Crop Insurance, Micro-insurance, etc. can help distribute the risk
- Local development facilitators and support groups play a crucial role in guiding small farmers manage their agro-enterprise
- Improve value chain financing through capacity-building of rural finance players particularly the MFIs.



CONCLUSIONS AND FUTURE DIRECTION

- Private corporate markets need to be encouraged to accommodate the produce of small farmers under a competitive arrangement. There are clear advantages both to the farmer and institutional buyer that can be maximized.
- Business trust, quality assurance, and supply reliability has to be established by the farmers in order to ensure this farm-to-market institutional arrangement.



CONCLUSIONS AND FUTURE DIRECTION

- Government support must remain in the areas of capacity-building, research and technology, infrastructure, wholesale financing, insurance and guarantees



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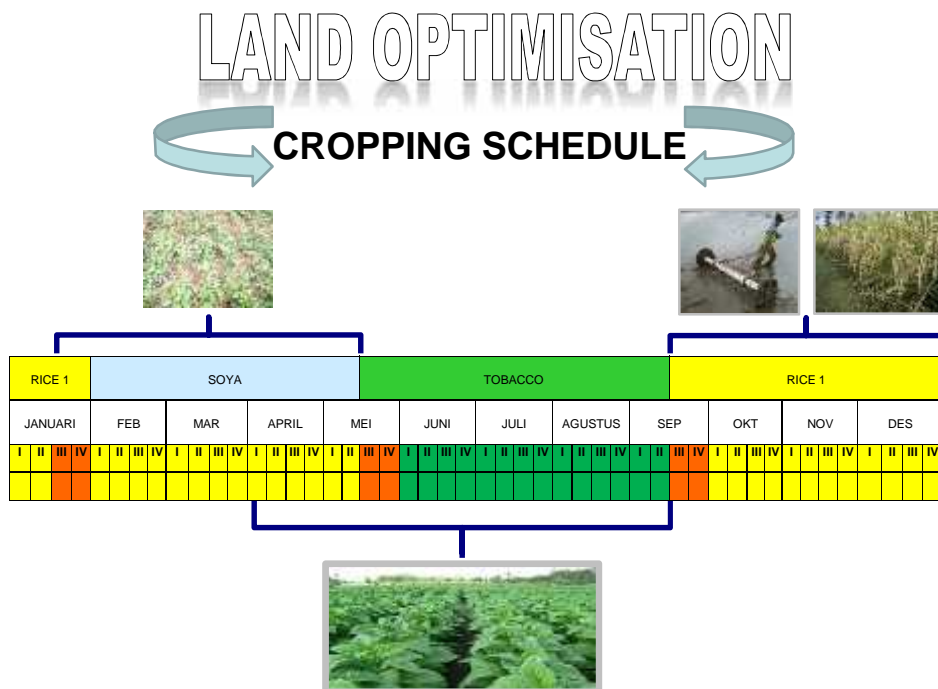
Challenges facing smallholder farmers in Indonesia

- Land Tenure (plots too small, not viable)
- No young people going into farming or agricultural management.
- High risk and hard work (drudgery)
- Lack of investment into smallholder agric, no Long Term approach (Pvt and Govt)
- Market stability (commodities and currency)

MIXED FARMING IN LOMBOK (INDONESIA)

- TOBACCO
- RICE
- MAIZE / SOYA
- GOATS/ CATTLE / CHICKENS
- FORESTRY (ACACIA–SESBANIA SP.)
- FINANCE & MARKETS





FARMER PROFILE

FARMER NAME : HAJI PINTAR
FIELD TECHNICIAN : AFAN.. RAJIN
LAND AREA : 0.33 Ha
LAND RENTAL : 0.67 Ha (\$ 1000/Ha/Tobacco Season)

CROP YEAR 2009

Crop	Land Area (Ha)	Other	Land Rental 1 Year (Rp)	COP Inputs (Rp)	Yield (Kg)	Selling Price (Rp/Kg)	Total Return (Rp)	Crop Profit (Rp)	Actual Return (Rp)
Rice	0.33	-	-	2,640,000	2,000	2,000	4,000,000	1,360,000	-5,340,000
Tobacco	0.33 + 0.67	-	6,700,000	33,000,000	2,100	27,000	56,700,000	23,700,000	23,700,000
November (2000 Trees)	-	2000 Trees	-	300,000	-	-	-	-	-300,000
SUM PROFIT				35.940.000			60.700.000		18,060,000

Objective : Use profit to rent land
Plant Trees

- Land for 1 year not seasonal





November 2009 Planting Sesbania

- Forestry
- Livestock feed
- Tobacco Curing
- Reduction in Deforestation

- +/- 2 M Trees Planted in 2010 – 2013
- 2014 Plant 2M Trees





CROP YEAR 2010

Land Rental : 0.67 Ha (\$ 1500 /1 Ha / 1 Year)

Crop	Land Area (Ha)	Other	Land Rental 1 Year (Rp)	COP Inputs (Rp)	Yield (Kg)	Selling Price (Rp/Kg)	Total Return (Rp)	Crop Profit (Rp)	Actual Return (Rp)
Rice	0.33+0.67	-	10,050,000	8,000,000	5,500	2,250	12,375,000	4,375,000	4,375,000
Tobacco	0.33+0.67	-	-	36,000,000	1,900	23,500	44,650,000	8,650,000	8,650,000
Sesbania 1 Year Old	-	2,000 Trees	-	-	-	-	-	-	-
PROFIT SUM				44,000,000			57,025,000		13,025,000

Objective : Focus and Manage All Crops Correctly

- 2010 was a bad year for tobacco
- Land rental for 1 year
- Trees all already 1 year old
- Profit in 2010 used to rent land in 2011



LAND RENTAL: 0.67 Ha (\$1500/Rp 15 M/1 Ha / 1 Year)

CROP YEAR 2011

Land Rental : 0.67 Ha (\$1100 /1 Ha / 1 Year)

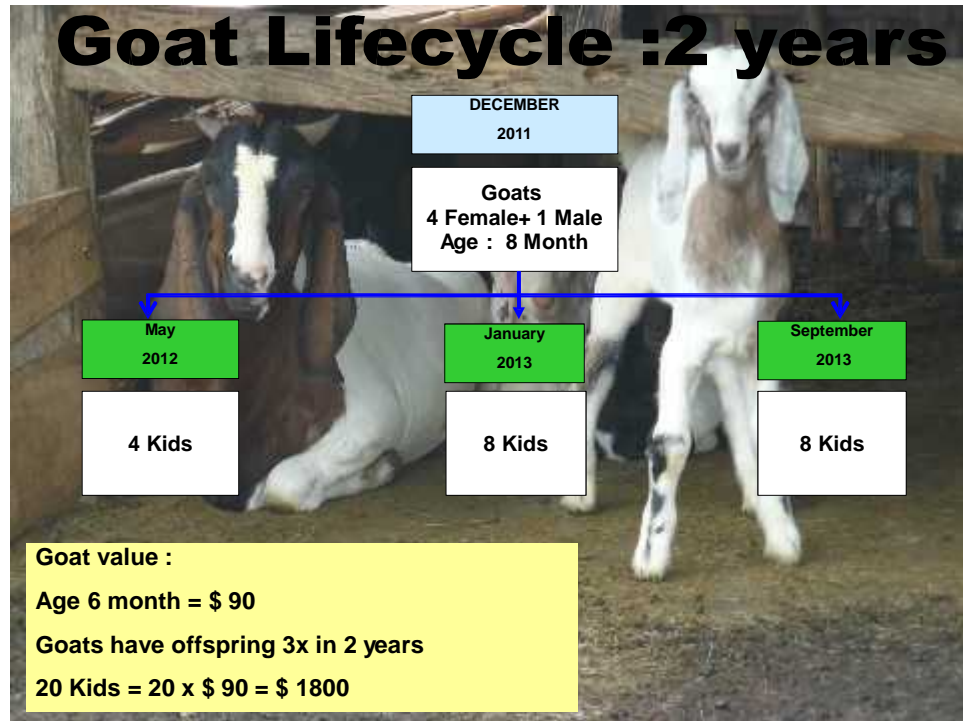
Crop	Land Area (Ha)	Sum Goats, Sesbania	Land Rental 1 Year (Rp)	COP Inputs (Rp)	Yield (Kg)	Selling Price (Rp/Kg)	Total Return (Rp)	Crop Profit (Rp)	Actual Return (Rp)
Rice	0.33+0.67	-	7,370,000	10,000,000	7,000 <div><div></div></div>	2,500	17,500,000	7,500,000	7,500,000
Tobacco	0.33+0.67	-	-	38,000,000	2,300 <div><div></div></div>	30,000	69,000,000	31,000,000	31,000,000
Sesbania 2 year old	0.33+0.67	2,000 Trees	-	-	-	-	-	-	-
Bought Goats		1 Male		1,800,000					-1,800,000
		4 Female		3,000,000					-3,000,000
		Stable		1,400,000					-1,400,000
PROFIT SUM				54,200,000					32,300,000

Objective :

-Sesbania 2 year old used to feed livestock

- Profit from 2011 : - Rent Land 2012 / 1 Year

- Buy Goats 4 female + 1 male



Goats Eating Sesbania



Land Rental : 0.67 Ha (\$ 1500 /1 Ha / 1 year)

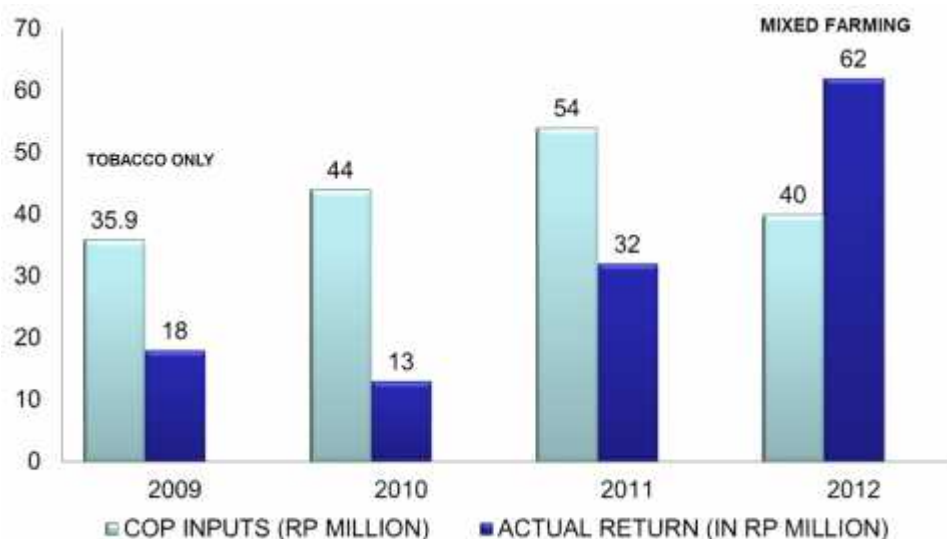
CROP YEAR 2012

Crop	Land Area (Ha)	Sum Goats, Sesbania	Land Rental 1 Year (Rp)	COP Inputs (Rp)	Yield (Kg)	Selling Price (Rp/Kg)	Total Return (Rp)	Crop Profit (Rp)	Actual Return (Rp)
Rice	0.33+0.67	-	10,050,000	10,000,000	7,000	2,500	17,500,000	7,500,000	7,500,000
Tobacco	0.33+0.67	-	-	30,000,000	2,300	30,000	69,000,000	29,000,000	29,000,000
			(40,000,000-10,000,000 (wood))						
Sesbania ready to Harvest	0.33+0.67	2,000 Tress	-	0	72 MS	275,000/SM	19,800,000	19,800,000	19,800,000
GOATS		1 Male							-
		4 Female		0	10 Kids	900,000	9,000,000	6,000,000	6,000,000
Profit Sum				40,000,000					62,300,000

Objective :

- Sesbania ready to harvest after 3 years – saves on curing fuel or for sale to other tobacco farmers.
- Goats ready for sale
- Increased profit can be used to rent land for longer periods.
- Land tenure is the major challenge facing Indonesian Small holders

SMALL HOLDER RETURN WITH MIXED FARMING



Requirements for smallholder sustainability

- Appropriate Government support
- Land Tenure settlement and stability
- Training for farmers and field staff
- Investment by private sector
- Local content requirement
- Infrastructure and mechanisation
- Cheap accessible finance
- Market access



Contract Formation and Obligations of the Parties

Lesson Learned and Experiences from Lao PDR

Presented at:

Workshop on the Legal Dimension of Contract farming
26 September, 2014, Bangkok

By

Souvanthong Namvong
Department of Agriculture Extension and
Cooperatives (DAEC)



Outline of Presentation

- Overview of Lao PDR
- Background - Contract farming in Lao PDR
- Role of different stakeholders
- Lesson Learned - Factors for success
- Recommendations

Overview of Lao PDR

MAP of LAO PDR

- Population about 6.5 M
- Areas: 236,800 sq KM

Land locked but land linked
country

Agriculture Sector

- Transition from subsistence to commercial production
- Transition from public service providers to resource linkers and facilitate farmer organisation development



Background - Contract farming in Lao PDR

- A rapid rise in contract farming in Lao PDR due to improved infrastructure and promotion of commercial agriculture
- Types of contract farming in Laos
 - 2+3 (quite know well)
 - 1+4
 - Informal contract or contract by hearth/trust



Roles of different stakeholders

Roles of buyers and farmers

Companies	Farmers
1. Data collection in the village	1. Land ownership
2. Given their policy to the government office and farmers/producer groups	2. Self-produce but sell to company
3. Provide inputs	follow contract 3. Provide labor
4. Provide tools in production and technical advice/training Jointly organize producer groups some time including government staff	4. Strictly in contract agreement: quantity/quality of productions
5. Put down guarantee money for contract	5. Feedback meeting after end of season to draw lesson learned
6. Buy back per contract	6. Negotiation with buyer in next season based on lesson learned
7. Summarize constraint in investment	

Roles of different stakeholders

Roles of local authorities (LOs)/facilitator

- Pay attention to give opportunity for both parties for open dialogue and negotiation.
- In the beginning, LOs provided information to farmers - both on advantages and risk in joining contract farming.
- To build trust between investors and producers
- Encourage investors to invest to create employment and generate income – by allocating area for production,
- Advice and train farmers
- Facilitating for import of inputs and export productions
- Follow up the contract enforcement
- Organise the evaluation workshop during the end of season



Roles of different stakeholders

Example in Bounea district

- Roles of each sectors

DAFO	Commerce	Finance	Environ & Nat. Res	Cluster / Village
Direct in production	Direct in import and export	Direct in fee collection	Direct in environment	Lead producers in production
Define policy: type of investment and technical	Define standard of products	Define fees	Define area	Mediation in conflict
Mediation in conflict	Mediation in conflict	Collect export taxes	Mediation in conflict	
Participate directly in contract with companies	Participate directly in contract with companies	Participate directly in contract with companies		
Organize annual evaluation	Pay guarantee money to farmers in case of damaged	Pay guarantee money to farmers in case of damaged		

Arbitration and dispute settlement

- Mutual agreement between farmers and investors
- Agreement mediated by village authorities
- Agreement mediated by parties signed as witness at the district level
- Agreement mediated by a lawyer
- Economic dispute settlement Office of Justice Division at the province, Vientiane Capital or the Ministry of Justice
- By the People Court, with both parties using lawyers

Informal and Semi formal

Formal but not much practiced

Lesson Learned

- Factors for success

Farmers are organized and can negotiate with investors
e.g. prices, policy

LOs provide adequate information for decision making to
both investors and farmers

Investors follow contract and have plan to establish long
term partnership with farmers

Guaranteed deposit from investors


Marketing

- Price
- Competitions
- Facilitators
- Dependency
- Natural disaster



Recommendations

- Participation in contracting farmers must be voluntary for those interested and should make their own decision.
- Farmers and investor should have power in decision making
- Division of responsibility should be in detail such that each sector understand clearly and follow
- Content of contract have to be developed in consensus among investor and farmer facilitated by a third party e.g.; local authority
- Regular monitoring, evaluation and draw lesson learned



Thank you very
much for your
attention!

NOTES FOR THE CONSULTATION WORKSHOP ON THE UNIDROIT / FAO LEGAL GUIDE ON CONTRACT FARMING

Tony Salvador *

Taken from "A Destiny of Debts Unmasking the Prejudicial Contracts in the Banana Industry in the Philippines", publication of the Initiatives for Dialogue and Empowerment through Alternative Legal Services (IDEALS), January 2014

Summary

Banana farmers and growers, even when they form part of a cooperative, are often exploited by corporations who foist upon them unfair terms and conditions of contract farming. Prices paid to farmers are low, even as inputs are charged to them by the corporations, albeit without the benefit of informed judgment and prior consent. Also, risks of rejection by the buyers abroad are unjustly passed on to the farmers, even **after** the corporations had already assumed possession and ownership of the produce. However the farmers are not given their fair share when the corporations benefit from increase in prices.

Tragically, farmers and their cooperatives end up in debt, out of which it is often impossible to get out of. Thus, while they may have acquired title to the land through the agrarian reform program of the government, after long years of struggle, beneficial ownership of the land is effectively reclaimed or taken over by corporations.

It is crucial then that governments and even NGOs provide the proper training to farmers and their organizations so that they are able to bargain for better terms in their contract farming agreements.

Thereafter, enforcement of these contracts must be ensured by providing adequate legal assistance to farmers and by marshaling government resources, such as, in the case of the Philippines, those of the Department of Agrarian Reform, the Department of Agriculture, and the Department of Justice.

In the meantime, all of these types of support are also crucial for the farmers to get rid of the current unjust contracts that had been foisted upon them.

BACKGROUND OF THE STUDY

The banana industry's contribution to the Philippine economy cannot be ignored. Except for typhoon-induced drops in production, the industry has shown consistent growth of about 6.4% every year, reaching 9.101 million metric tons produced in 2010. On the same year, 8.5% of all agricultural produce were bananas, amounting to about Php106.billion¹. Exports exceeded US\$360 million and accounted for about nine percent (9%) of the country's total agricultural export value.

* Legal Consultant, Asian Farmers Association (AFA)

¹ Approximately, US\$1.00: PHP44.43 as of 25 September 2014. The rest of the footnotes are omitted.

In 2013, the Initiatives for Dialogue and Empowerment through Alternative Legal Services (IDEALS) studied various contracts involving banana growers in Mindanao. This study is part of an ongoing research and empowerment initiative aimed at surfacing and addressing the vulnerabilities of agrarian reform beneficiaries in their contractual dealings with multinational corporations and large exporters.

While many provisions in the various studied contracts were regular and even beneficial to all parties concerned, some contractual terms are highly questionable. As a result, further research was made to review existing literature on the conditions of banana farmers in the Philippines.

This Policy Note will focus on growership contracts.

ISSUES TO BE DISCUSSED

- Do banana farmers really earn well from producing bananas that are exported to the world?
- Why are some Filipino banana farmers drowning in debt?

Why are banana farm-gate prices so low?

Prices remain very low because of two factors.

1. No standard price guides and lack of reliable information regarding fair market prices

Government regulation ² requires parties to growership contracts, including those in the banana industry, to follow this provision:

*"The production/contract growing/growership/marketing contract shall stipulate the terms of sale which shall include the quality, quantity, and price of agricultural produce to be bought by the investor."*³

However, a review of the same regulation reveals that there are no guidelines given so that the parties can arrive at a fair price. As a result, when farmers appear at the negotiation table, they have no base price to work with other than their knowledge of the prices received by cooperatives in neighboring farms. While this information may be useful, it does not translate into a legal obligation that would bind the corporation.

When some farmers mentioned the prices received by other cooperatives, they were simply informed that the company they were dealing with was not as big as the company in the neighboring town and thus cannot offer the same prices for the same type of banana produced.⁴

The lack of an industry and government standard for setting prices in the banana industry greatly encourages that take-it-or-leave-it attitude that prevails among corporate buyers. As the weaker party in most contractual negotiations, farmer-cooperatives are often left with no other choice but to accept unjust terms.

It should be mentioned that IDEALS has been actively participating in the drafting the competition policy bill in the Philippine Congress. One of the issues that we had successfully fought for is

² Department of Agrarian Reform Administrative Order No. 9-06, December 8, 2006.

³ Id., section 5.2.1.

⁴ Interviews conducted on 15-16 October 2014 with HARBCO and DFC cooperative-members.

prohibition of MONOPSONY, where a single buyer or a cartel of buyers are able to force marginalized or poor producers to sell their products at an unfairly low price.

2. Price review mechanisms do not work, are improperly used, or simply ignored.

Government regulation requires parties to incorporate a price review mechanism in growership contracts. It states:

“5.2.8. The agreement shall incorporate a price review mechanism, including the disclosure of prices and post-harvest and marketing cost, taking into consideration industry practice, prevailing market prices, and other appropriate factors.”

This is a sample provision of a contractual price review mechanisms:

“3. There shall be a price review at least every two (2) years or sooner should there be an increase of 5% in the price of imported materials, such as fertilizers, herbicides, fungicides, insecticides and others, either or both parties may call for a price review.”

Clearly, price reviews depend solely on the parties to the contract: the farmer-cooperative and the investor-corporation. Most of the time, they do not work because the information needed to change the price in the contract is unavailable. Information on prevailing market prices are not easily accessible and often are not even published.

Even information on the prevailing prices of imported farm inputs is not easily accessible. As a result, price reviews often do not occur. One party, i.e. the corporation, simply invokes that the conditions necessary to trigger a price review do not exist.

Unfortunately, by classifying the process of price reviews as a contractual matter, farmer-cooperatives are forced to file cases and invoke a breach of contract. Often, this is a remedy left unused because farmers cannot afford to bear the cost of litigation.

Without a working price review mechanism, farmers are often locked into five to ten year contracts that set state prices which may have been fair in the year 2000 but definitely are oppressive in the year 2013.

Why are farmers drowning in debt?

1. Low prices in growership contracts.

The prices set in most growership contracts in the banana industry are already extremely low. Unfortunately, farmers get net returns only after automatic deductions of various items (i.e. production cost).

In the production of Cavendish bananas, the estimated production cost may be broken down into the following items⁵:

⁵ Digal (2005) cited in Joy Hasmin De Los Reyes and Wim Pelupessy, Agrarian Reform in the Philippine Banana Chain, University of Antwerp, Institute of Development Policy and Management, Discussion Paper 2009-03.

Item	% of the Total
Labor	36.9
Fertilizers	8.0
Pests and disease control materials	27.9
Bagging materials	6.1
Propping materials	4.9
Fuels, oils, lubricants	4.7
Depreciation 8.4	8.4
Overhead	3.1
Total	100

As a result, farmers get very little for every box of bananas that they produce. In fact, HARBCO even alleges that:

"Consistently, from December 2008 and up to the present, the gross sales, out from the purchases made by LFC of the bananas it actually produced from the HARBCO farms, had been less than the gross production costs incurred by HARBCO out of the same period."

While the banana export industry is experiencing significant growth, many farmers are saddled with insurmountable debts. This section highlights contractual provisions found in the Exclusive Production and Sales Agreement between Sumifru (Philippines) and various ARBs (dated 23 June 2008), General Framework on Farm Handling between Lapanday Foods Corporation and Hijo Agrarian Reform Beneficiaries Cooperative (HARBCO) [dated 23 December 2008], and Banana Sales & Marketing Agreement between Hijo Plantation, Incorporation (now Lapanday Foods) and HARBCO (dated 28 December 1998).

For example, the Hijo Agrarian Beneficiaries Cooperative (HARBO) currently owes its contractual partner, Lapanday Foods Corporation, the shocking amount of Php 414.35M. In its petition filed before the Department of Agrarian Reform Presidential Agrarian Reform Council, HARBCO alleges that:

This outstanding debt was more of the result of the unrestrained authority of LFC to incur production costs and expenses which the company is allowed to charge to the account of the HARBCO and deducted from the sales proceeds of the bananas of HARBCO, which are purchased by LFC based on its own price mechanisms.

These unfavourable conditions found in the GFFH and other contracts have actually buried the HARBCO in a "cycle of debt". (emphasis supplied)

The cycle of debt scenario is common. For example, some farmers in partnership with **Sumifru** Philippines, are currently applying for financial assistance from the Land Bank of the Philippines. Pending approval of their application, the farmers narrated that the company continues to charge certain production costs, including those spent for aerial spraying, despite the fact that they have ceased operating since December 2012 when Typhoon Pablo damaged their farms.⁶

⁶ Supra note 4.

2. **Common Debt-creating Contractual Provisions**

Farmers pay for most of the things needed to produce bananas, at prices often determined solely by the company-investor.

First of all, government regulations allows investors to “provide at reasonable cost, the technology and other farm inputs prescribed for the production of agricultural goods according to the quality standards set by the growership contract”⁷. Furthermore, “The schedule of deduction and amounts representing the cost or value of the use of the technology, equipment, facilities, service and other farm inputs provided by the investor to the beneficiaries shall be agreed upon by both parties and shall be clearly stipulated in the contract.”.

Initially, these two provisions appear beneficial for the farmers. Often, they cannot afford to make advances or pay for farm inputs before they get paid for the harvest. Their company investor can make these advances and get paid through automatic deductions from payments due to the growers.

Unfortunately, while contracts do contain provisions enumerating what may be charged to the account of the farmers, provisions on the schedule and amount of such automatic deductions are absent.

As a result, farmers are made to pay for the following:

- farm inputs and materials at competitive market price;⁸
- prevention and control of insect, diseases, and pestilence;⁹
- irrigation, cable harvest and overhead cable propping systems;
- hiring of emergency or project workers and labors;
- umaintenance and improvement of canals and feeder roads on lands planted with bananas.

Moreover, farmers have very little control over the actual cost of the materials because:

- a) they have very little **information** and/or access to reliable information on competitive market prices, and
- b) they only discover how much the charges are when the companies send them the financial records.

3. **Absence of mechanisms to contest the amounts charged by the company-investors**

One company included the following transparency clause as regards costs chargeable to the growers: “Documentations as to costs incurred during LFC’s farm handling will be transparent and furnished to HARBCO.”

This provision does not reduce the debt of the cooperative because it does not include negotiations and consent before these costs are incurred. The farmers are simply informed that the company paid for certain material inputs and that the farmers are liable to pay for them at a certain amount that is solely determined by the corporation.

⁷ Supra note 2, Section 5.2.2.

⁸ 1General Framework on Farm Handling between HARBCO and Lapanday Foods Corporation, 23 December 2008.

⁹ Exclusive Production and Sales Agreement between various ARBs and Sumifru (Philippines), 23 June 2008.

It is also clear that the process of contesting the prices set by the investors is hard or even impossible for farmers to access. For example, the contract between HARBCO and Lapanday Foods Corporation provides that disputes arising from their contract “shall finally be settled under the Rules of Conciliation and Arbitration of the International Chamber of Commerce.” Conciliation/mediation is the choice of dispute resolution for Sumifru (Philippines) but even this has become very difficult for the farmers who cannot afford the services of a lawyer to guide them through the mediation/conciliation proceedings.

4. **Farmers are liable for losses beyond their control.**

Aside from the burdensome automatic deductions that farmers bear during each harvest, certain contractual provisions on liabilities further worsen their economic conditions.

For example, Lapanday requires the farmers to **“replace bananas rejected in any port and/or by the foreign buyers on account of poor quality or non-compliance with the quarantine regulations,”** “yellow bananas” or other conditions that necessitate their disposal.”¹⁰

This extension of liability for rejections made in foreign ports is unreasonable and senseless considering that Lapanday’s own contract allows them to reject the bananas “at any time prior to BUYER’s [Lapanday] acceptance of the bananas loaded on board the Buyer’s designated cargo truck”.¹¹

The same provision exists in the Sumifru contract:

“At no cost to the Company, the Growers shall replace Crops rejected in any port and/or by the foreign buyers on account of poor quality or non-compliance with the quarantine regulations and other conditions that necessitated their disposal or made them unacceptable, which conditions were not visible or detectable at the time.”

It is obvious that the partnership between many corporations and the grower-farmers is extremely detrimental to the farmers. Corporations do not share their export gains with the farmers because purchase prices are pre-determined in the contract. However, losses are borne solely by the growers.

In order to avoid passing the risk of rejection of goods to the farmers, corporations must also be responsible in ensuring that the bananas they accept from the farmers and subsequently ship to foreign markets are compliant with the market specifications and conditions.

Other factors like shipping conditions, length of travel, and port handling affect the conditions of the bananas shipped to foreign markets. It is highly unreasonable for farmers to be made liable for damage that may be incurred due to those factors outside their control. In the case of HARBCO, the company even failed to pay for land amortizations despite a contractual provision imposing this obligation.

As of 31 August 2013, the total unpaid obligation of the cooperative has reached the sum of PHP199,451,826.66, or around US\$450,000.

¹⁰ Banana Sales and Marketing Agreement between Hijo Agrarian Reform Beneficiaries (HARBCO) and Hijo Plantation, Incorporated (now, with Lapanday Foods Corporation), December 28, 2008, Part IV, k.

¹¹ Id., at Part IV, j.

What can be done? Recommendations

Establish proper access to information. Government, through extensive consultations with farmers and investors, must come up with guidelines so that purchase prices for bananas are fair, humane, and competitive.

Government, through the Department of Agriculture and the Department of Trade and Industry, must regularly release information on the prevailing market prices of different farm inputs. Considerable efforts must be made so that farmers and investors alike will have access to these types of information. Government must conduct a thorough review of agribusiness venture arrangements (AVAs) involving agrarian reform beneficiaries.

Establish a business climate built on conditions of fairness. Companies should not be allowed to unilaterally set purchase prices to the detriment of the farmers. For the Philippine banana industry to continue its significant growth, it must operate on conditions of fairness.

While company-investors may purchase farm inputs and charge them to the growers, the latter should be given the chance to negotiate with the companies before these purchases are made. Growers should likewise be permitted to buy from sources that offer lower prices.

The Department of Agrarian Reform, in Administrative Order No. 09-06, 23 states:

“To augment the support services extended by the government to the agrarian reform beneficiaries (ARBs), the formation of agribusiness venture arrangements is encouraged as a means by which investment of financial and other resources by the private sector can be channeled to agrarian reform areas through productive and collaborative ventures between the private sector and the ARBs.”

Provide regular training and support to farmers. Growers in turn must be given regular trainings and technical/capacity building support so that they can improve the quality of their produce.

The rules of the international agricultural market are constantly changing and consumers are becoming more discerning as regards food products. For the Philippine banana industry to remain competitive, farmers must constantly adjust to the demands of the market in terms of quality standards.

Agri-venture agreements (AVAs) involving Agrarian Reform Beneficiaries (ARBs) must be evaluated.

Government must conduct a thorough review of agri-venture agreements involving agrarian reform beneficiaries.

With the ever-increasing complaints against unfair contracts, government, through the Department of Agrarian Reform, Department of Agriculture, and the Department of Trade and Industry, must check if indeed the provisions of these agreements fairly and justly represent the interests of both the farmers and the corporations.

The DAR must also strictly implement the provisions in its own regulations requiring AVAs to go through proper evaluation by the National AVA Evaluation Committee-Technical Working Group.

Conclusion

Lacking the ability to undertake a thorough review of the contracts and the ability to understand the regulations that govern the relationship between farmer growers and investor-companies, the farmers will continue to suffer the direct effects of unfair pricing and cyclical debts. Instead of improving their economic status through productive use of their lands, they will forever till their own lands under conditions of contractual slavery.

No matter how well it is performing in the international and domestic trade arena, an industry must not be allowed to thrive if it cannot ensure fair, humane, and just conditions for the vital movers of its production chain: the farmers.

The food that we eat must reach our tables without sacrificing the lives of those that till the land and grow the things that nourish us. Contracts that violate human dignity have no place in the modern world.

September 25, 2014



MALAYSIA'S CONTRACT FARMING CHALLENGES

"A CASE STUDY"

DATO' AB RAHMAN B ISMAIL

GENERAL MANAGER

NATIONAL FARMERS ORGANIZATION (NAFAS)

MALAYSIA



NATIONAL FARMERS ORGANIZATION INTRODUCTION

"National Farmers' Organization" :

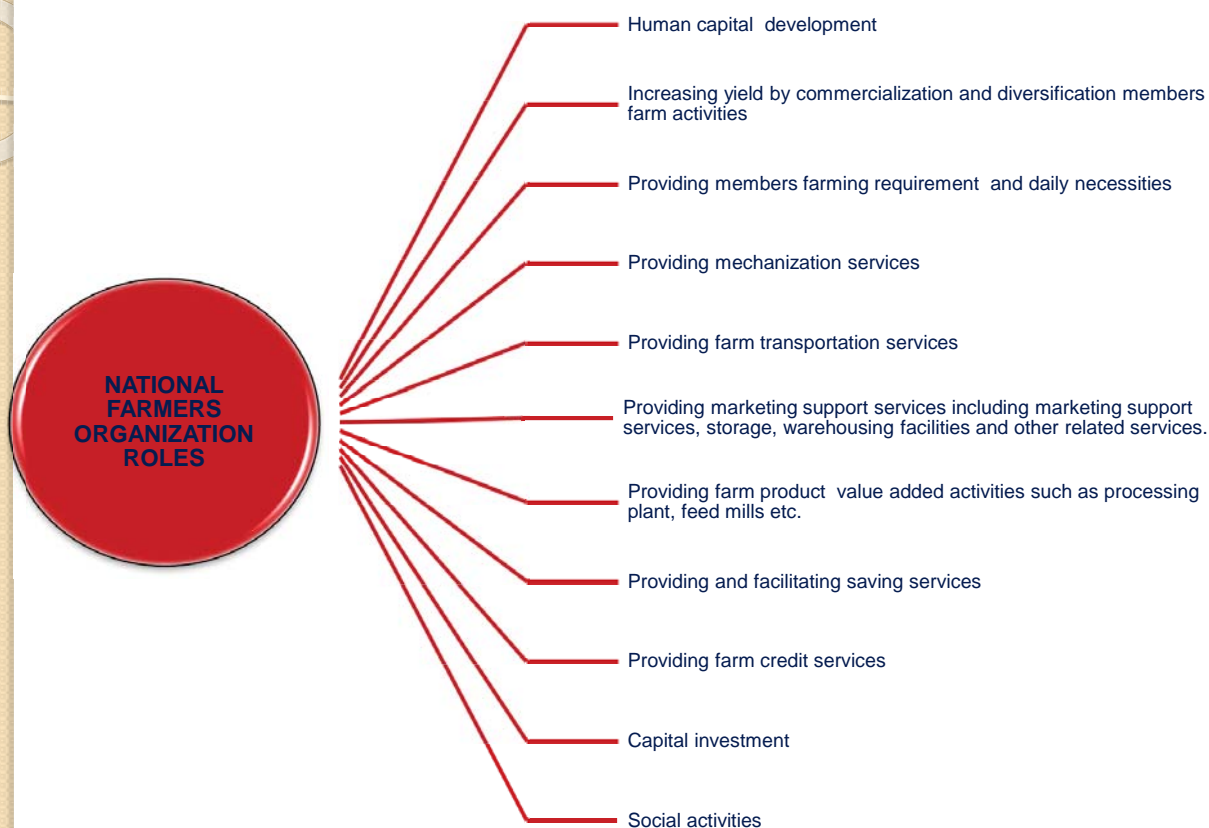
- Malaysian Farmers Organization movement apex cooperative
 - 14 State Farmer Organization (SFO)
 - 177 Area Farmer Organization (AFO)
 - 826,000 Members



NATIONAL FARMERS ORGANIZATION

OBJECTIVE

- ❑ To improve members social and economy status;
- ❑ To improve members knowledge and skills;
- ❑ To Increase revenue and income; and
- ❑ To improve members way of life by developing a progressive, independent, prosperous and united farming community.



NAFAS POULTRY CONTRACT FARMING



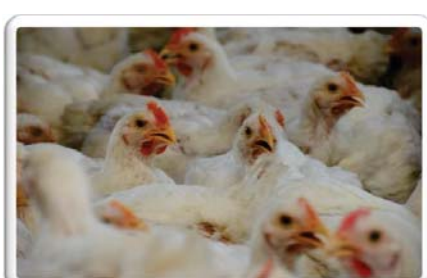
NAFAS POULTRY CONTRACT FARMING

“ an integrated, organize and controlled
poultry project by Farmer Organization
movement “

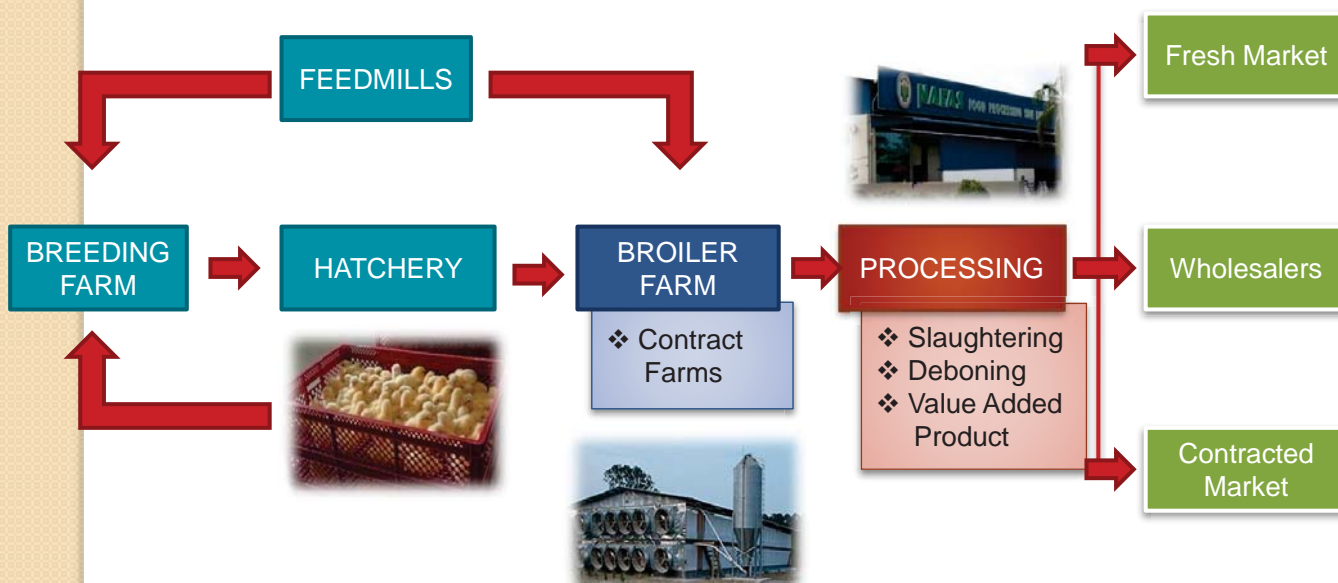


PROJECT OBJECTIVE

- ✓ To increase income
- ✓ To sustainable income
- ✓ To secure poultry supply
- ✓ To get consistent supply
- ✓ To get quality of chicken

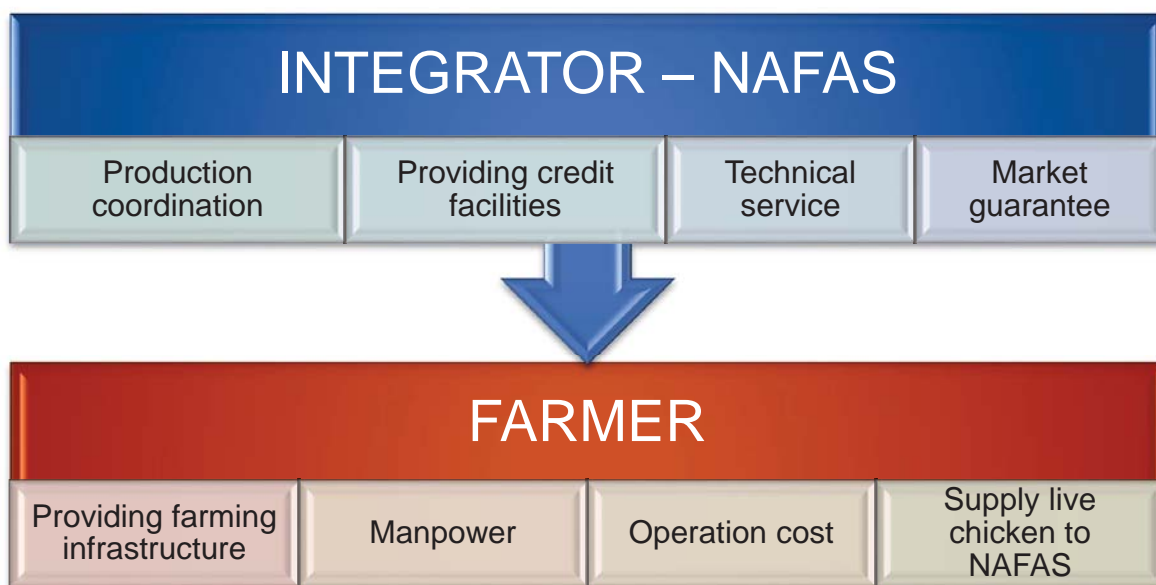


PROJECT VALUE CHAIN



“FROM FARM TO TABLE”

FARMING ACTIVITIES



WAY FORWARD

- To enhance and strengthen the project value chain
- Reducing cost of production
- Develop a new market focusing on value added activities





THANK YOU

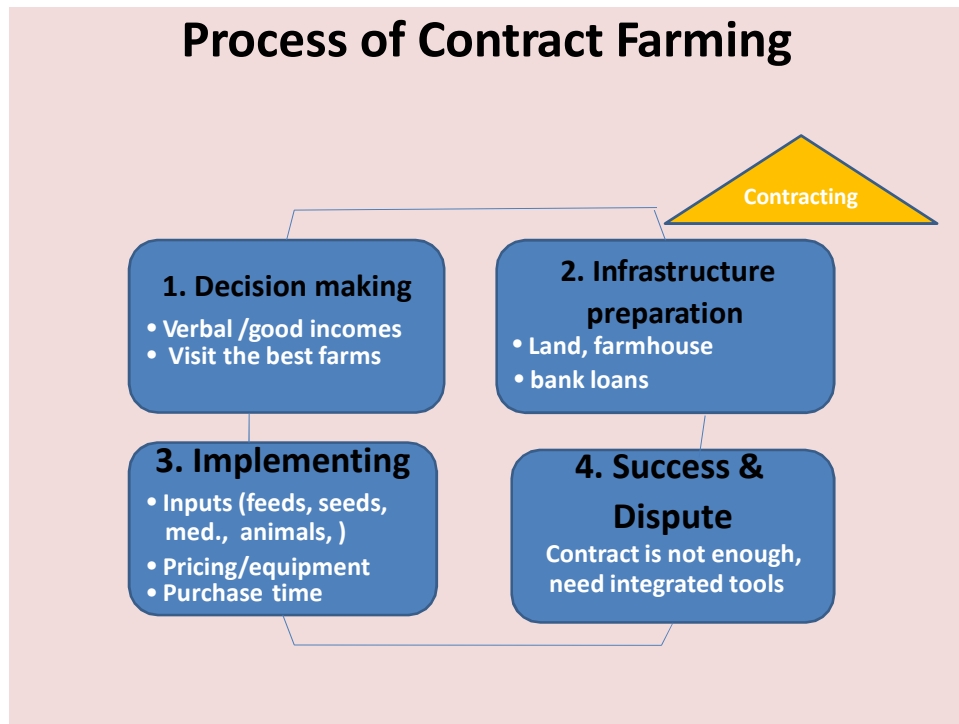
“The Justice for Better Life in the Fair Contract Farming System in Thailand”.

Implementing partners:

- 1. academic institutes,*
- 2. farmer-producers,*
- 3. NGOs*
- 4. GOs concerned*
- 5. The Law Reform Commission of Thailand.*

The project main purposes are

- 1) *legislation process*** on issuing the Act on Protection Farmers/Producers in Contract Farming
- 2) *capacity building for the leaders of farmers/producers’ group/network*** and consumers leaders and network on the project titled “On the Path to Leadership and Change Agents in Contract Farming”
- 3) *Policy advocacy and campaigning*** on “the Healthier and Better-Contract Farming”;
 - 1.1. *Ministry of Labour*** -- labour protection on fair wage, employment pattern and occupational health & safety;
 - 1.2 *Ministry of Agriculture*** -- production and lowering the production costs;
 - 1.3 *Ministry of Justice*** -- fair mechanisms for justice in the CF system.



A more “fair” contract farming systems in Thailand ?

- The illiteracy and literacy but non-negotiable conditions of the producers are the main problems.
- The institutional settings (policy and compliance by state agencies) are not able to and not ready to protect the producers but the buyers.
- The ambiguity of state responsibility makes the solutions are less possible due to no assignment. Once the problem occurs, it is often treated as the “None-of-My-Business”.
- Because of related complexity of the contract farming system (i.e. authority, responsibility, information, database, legal aspects), these lead to the most complicated dispute resolutions which are unmanageable by only a sole agency.

Contract farming in Thailand

- The unequal power in negotiation between the producers and the buyers
- the contracts become a serious tie and a powerful tool in controlling and punishing the producers in terms of suing, fine and putting them in debt.

Why not end the contract?

- The most contracts applied in the contract farming in Thailand are under asymmetric style.

Termination of the contract means:

- Pay all debts

Dispute resolution mechanisms

- 1) to establish an Act on the Contract Farming Producers' Protection and the Development
- 1) to establish a fund for risk management, guarantee in terms of disaster, loss and revival funding,
- 2) to support the empowerment of the buyers in sharing information, resources; capacity building and networking at the regional and the national levels.

DISPUTE SETTLEMENT OF CONTRACT FARMING

LEGAL PRACTICE IN VIETNAM

Agriculture plays an important role in the Vietnamese economy due to the large number of people living in rural areas. It is, however, surprising to face the reality that contracts are lacking in agricultural transactions. Therefore, it is hard to settle disputes arising between the parties during the implementing these transactions. Furthermore, legal provisions regulating contract farming in Vietnam do not focus enough on settling disputes between the parties but rather rely on general legal provisions on dispute settlement. Generally, in order to resolve disputes where the parties cannot negotiate or conciliate, an adjudicating state agency or organization is required.

Under Vietnamese law, foreign investors and foreign-invested companies have the right to select the court of Vietnam, Vietnamese arbitrators, foreign arbitrators or the arbitrators appointed by the parties, to resolve disputes concerning investment activities in Vietnam. With respect to the disputes between foreign investors and the State management authorities of Vietnam, the parties will have to refer the dispute to either an arbitration body or court of Vietnam.

I. GOVERNING LAWS ON CONTRACT FARMING IN VIETNAM

Under the Vietnamese legislation, regulations regarding contract farming can be found in Civil Code, Trade Law and some specific regulations.

1. Civil Code 2005 and Legal Procedural Code 2004

In Vietnam, the Civil Code is considered as a general legal framework for contracts including agricultural contracts. Therefore, the provisions on dispute settlement are also used to solve disputes arising between the parties.

2. Trade Law 2005

The Law on Trade of 2005 covers the commercial activities of traders with a set of principles and stipulates specifically the regulations related to the purchase and sale of goods. Chapter II includes the general provisions, forms of contracts, the rights and obligations of the parties to contracts for purchase and sale of goods, and the purchase and sale of goods through the goods exchange. However, as the Trade Law requires only at least one party to the transaction to be a trader, and the role of the contractor fulfills that requirement, those provisions of the Trade Law are applicable.

3. Decision 80/2002/QĐ-TTĐ

On 24 June 2002, Decision No.80/2002/QD-CP (“Decision 80”) was issued by the Prime Minister, on policies to promote contracting between agribusinesses and agricultural producers in Vietnam. It consists of ten articles that mainly regulate the forms, entry to and the performance of the sale contract of farm produce, policies of the government to encourage the contractors to enter into the farm product sale contract with the producers, remedies in events of default, and responsibilities of local governments as well as concerned ministries and associations. It is, however, lacking provisions for mechanisms to solve disputes between the parties except for a reference to applicable law on this issue.

4. Decision 62/2013/QD-TTG

The Decision 62/2013/QD-TTG (“Decision 62”) on the policy encouraging development of the co-operation and the linkage between the manufacture and the marketing of agricultural products and the construction of large fields. This Decision replaces the Decision No. 80/2002/QD-TTG from 2002. With ten articles, the new Decision provides various kinds of support to the linkage between farmer and contractor, including sanctions in case there is a breach of contract. However, similar to Decision 80, the provisions on dispute settlement of Decision 62 is non-detailed and referred to applicable laws on the same issues.

5. Circular 77/2002/BNN-TT, Decision 77/2002/QD-BNN and other legal documents

These documents are guidelines of Decision 80 on contract farming, in which, the Ministry of Agriculture and Rural Development asked traders to use the Sample Contract as their proposal. Actually, this Sample Contract includes only skeleton contents in the contract farming, for example, prices, delivery, and obligations. It also draws down the dispute settlement and compensation in contract farming.

Besides, there are several legal documents on agricultural contract having no specific provisions on dispute settlement, such as: Circular 04/2003/TT-BTC dated 10 January 2003 guiding Decision 80; Circular 15/2004/TT-BNNPTNT dated 29 April 2014 guiding Decision 62, etc.

II. BREACH OF CONTRACT

In practice, contract farming is an agreement (either verbal or written consent) between farmers and a Sponsor (processor, exporter, agency, and marketing firm) on various agricultural products such as fruits, vegetables, eggs, dairy, rice and so on. Generally, contract farming may be diversified into following categories:

– The contents of the farming contract:

- Market Access (Future Consuming) Farming Contract;

- Supporting Farming Contract; and
- Processing Farming Contract.

– **Structure of the farming contract**

- Intermediary (Agency) Farming Contract;
- Unofficial (verbal) Farming Contract;
- Inter-relation Farming Contract;
- Centralized Farming Contract; and
- Plantation Farming Contract.

Depending on the form of contract farming, there are possibly hundreds of reasons put into debates:

1. Commodity:

Numerous issues may result from the commodity, ex. the quality of the products, the required processing, ingredients and specifications. Please be noted that most of such objectives rely on traders' standards. Thus, it is too difficult for farmer to claim the traders on the breach of contracts.

Suggestion: we should clarify all of specifications and requirements in the contract farming and note that traders have to examine the quality of commodity every month or week.

2. Services provided:

The traders may provide various supplies to famers such as fertilizers, seeds, pesticides, extension services and quality monitoring. However, not all of them are included in form of contract due to the unpredicted occurrences. For examples, the occurrence of new insects invaded or the limited quality of seeds may damage the output quality. Whether the new insects are Force Majeure to be exempted duties or not? Who may bear for these responsibilities? Obviously, two parties possibly mutual agree to put those things in the contracts but the unpredicted occurrences are too broad to cover in the contract only.

Suggestion: the services provided must be specified in the contract directly, the duties of non-performance or violations also proposed.

3. Risks:

Poor crop management, natural calamities, pest epidemics, market collapse and price fluctuations are also the risks of contract farming. The crop insurance seems a possible solution. However, in Vietnam, it is unusual for farmers/traders to guarantee their crop by insurance. It seems non insurance institution providing such insurances. Consequently, who bear the risk if there are any force majeure or unpredicted occurrences?

Suggestion: the risk should be negotiated clearly in the contract.

4. Price:

In Vietnam, the Price is not really open market. A limited group of giant traders may control the price due to their discretion. When the price is down, the traders often reject the commodity due to the unjustified quality ground. Vice versa, when the price is up, the traders often delay to collect commodity and/or collect sooner than usual harvesting season. Unfortunately, it seems impossible to ask the rights of farmer toward their commodity's price. Farmers could not keep their products in the warehouse forever.

Suggestion: in order to balance the benefits of parties, the price should be fixed before entering the contract and negotiating right before each season rather than based on the open market.

5. Land:

Commonly, Centralized Farming Contract or Plantation Farming Contract enhances the long term capital investment in the farmers' land to improve productivity and quality of products. The Government of Vietnam also supports for this trend. However, in our sides, the scale of farming is really small and medium size. The long term capital investment's effects are belonging to the scale of the land farmers keep. As the result, the traders often breached the contract once they cannot centralize land for farming.

III. DISPUTE SETTLEMENT

Currently, the dispute settlement in contract farming may be settled through two mechanisms which are:

- Judicial organizations having binding decisions, including the Court of Vietnam and the Arbitration; and
- Others subjects having non-binding decisions, including Commune People's

Committee, Farmer Union and Inspection Agency.

Below is my explanation on the dispute settlement through such mechanism:

1. Judicial organizations having binding decisions:

a. The Court of Vietnam tk 123 yl on 9123 ais

In line with legal system revolution, there have been positive changes as to jurisdiction and procedures for promptly resolving disputes equitably and in compliance with the law. The court system of Vietnam is set up at various levels, with the Supreme People's Court as the highest, the provincial People's Court, the district People's Court and the Military Court.

Each level of the court will have different jurisdiction. The district court as the court of first instance has jurisdiction over cases involving disputes relating to commodities trading; service supply; distribution; representatives and agents; consignment; hire, leasing and lease purchase; construction; technical consultancy; conveyance of goods and passengers by railway and road.

The provincial court is the court of first instance hearing cases in investment, financing, banking, insurance, sale & purchase of stocks and bonds, exploration and exploitation, transport by air and sea, technology transfer, intellectual property rights, disputes between the company and its members or among the members. Additionally, the disputes which involves an offshore party (including foreigners, Vietnamese people not present in Vietnam and foreign agencies & organizations without a head office, branch, representative office in Vietnam at the time when the Court accepts the case for handling) or an offshore property; the resolution of a judicial authorization to the consulate of Vietnam abroad also falls under the jurisdiction of provincial courts. The provincial court also conducts appellate hearings or judicial review of cases which has been heard by the district court, but the appeal or protest is lodged with the latter court.

The Supreme People's Court is the highest judicial body, acting as the court of appeal reviewing the judgment of the court of first instance issued by the provincial courts and have the authority to review under retrial and judicial review procedures decisions of the lower courts which have been legally effective, but are found to be contrary to the law, or new circumstances exit.

In practice, this is the most popular judicial organization parties ask once any dispute arises. Although the expenses in Court are really low, the legal proceedings may last for years. Thus, when the value of the dispute is low, it may prevent the possibility of parties to put their cases into the Court.

b. Arbitration

In parallel with dispute resolution by courts, dispute resolution by arbitration is also applicable in Vietnam even though it is not common as with the cases settled by courts.

The legal system for arbitration activities has been quite fully set forth, and there is mechanism guaranteeing the execution of arbitration awards, thus increasing the effectiveness of dispute resolution by the arbitration. Vietnam's arbitrators have jurisdiction over commercial disputes. The arbitration body which is considered the most experienced and best recognized is Vietnam International Arbitration Centre (VIAC) in conjunction with the Vietnam Chamber of Commerce & Industry (VCCI).

In fact, this is the least judicial body Parties choose to apply due to the cost. For the arbitration, if two parties are organizations or enterprises, they often choose that. On the other hand, the farmers often deny this kind of settlement.

c. Foreign Court and arbitration

Principally, Civil judgments & decisions of a foreign court, foreign arbitral awards will be enforced in Vietnam only if they are recognized and put into effect by a court of Vietnam. The recognition and enforcement of civil judgments & decisions of the foreign court in Vietnam are conducted based on the principle as follows:

- Vietnam and the country which renders such civil judgment or decision have signed or acceded to international treaties on this matter; and
- The judgment is not prohibited by the laws of Vietnam from being recognized and enforced.

It should be noted that the court of Vietnam will not review contents of the case or dispute which has been resolved by the foreign court or arbitrator, but only examine and compare the judgment or award with the attached document with the law of Vietnam as to determine whether to recognize and enforce the judgment or award in Vietnam.

In my practice experience, I have not recognized any case like this in Vietnam until now.

2. Others subjects having non-binding decisions:

Similar to other contracts, dispute settlement mechanisms in agricultural contract have two types: binding and non-binding. A binding mechanism, as mentioned above, is the settlement of dispute under the Court and Arbitration. Non-binding mechanism is implemented in ways of negotiation and mediation of the parties under consultation and supervision of Commune People Committee, Farmer Union and Inspection Agency. This is a special mechanism proposed by the Ministry of Agriculture and Rural Development and its sample contract. This is most popular ways to settle the dispute.

The Commune People Committee and Farmer Union, which are close to activities of farmers, understand deeply real situation of farmers so they are able to consult the parties being in dispute. Inspection Agency is often a company which takes in charge for inspection only, so obviously, its decision is also non-binding.

The outstanding strong point of dispute settlement under Court and Arbitration in comparison with the non-binding mechanism is ensuring the enforcement of the judgment due to its binding element. However, time-consuming and complex-procedure characteristic fluctuate the parties on deciding it as settlement mechanism since agricultural contracts in Vietnam are usually in small and medium size. In contrast, dispute settlement under mediation and negotiation with short time frames and simple procedures are more suitable to the parties. This mechanism, however, also has short-comings. The lack of experience in solving high-value-contracts of relevant bodies causes difficulties for the parties during the negotiation process. Furthermore, the non-binding characteristic also causes fluctuation of the parties to choose this mechanism to solve the dispute.

3. Recommendation

Over decades from the improvement of contract farming, dispute settlement is still very simple, primitive and ineffective, thus a number of seminars and workshops have been organized to promote the dispute settlement mechanism. There are three major points as negative effects to current mechanisms, including:

- The authority does not play an important role in balancing the relationship between the farmer and the traders;
- The role of Authority, Farmer Union and others are dimmed; and
- Rules of Court, Arbitration and other legal mechanism are not positively effects on settling dispute in relation to agricultural sector.

With the mentioned reasons above, there is a need to create a mechanism to solve disputes relating to agricultural contracts due to its special characteristics. It could be implemented in these ways: (1) convert the non-binding mechanism into binding mechanism to ensure the enforcement of the parties; and/or (2) create a special jurisdiction body which has special procedure to solve the dispute for agricultural contract.

IV. RESULT OF DISPUTE SETTLEMENT:

Where there is a breach of contract, the violation party shall be asked

to: (i) compensation for the material damages/loss;

- (ii) penalty due to the provision of contract in accordance to category of the breach;
- (iii) stopping the breach behaviors and continuously carrying out the contract;
- (iv) terminating the contract; and
- (v) the Authority will terminate all support and sponsors (if any) to the violation party./.

DISPUTE SETTLEMENT OF CONTRACT FARMING

LEGAL PRACTICE IN VIETNAM

Prepared by: Mr. Tran Quoc
Dat - Deputy Director of Hiep
Tai Food Company Limited

September 2014

I. Category of farming contract

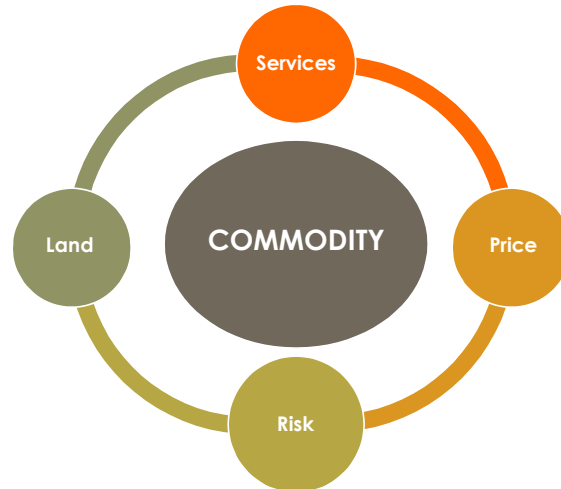
The contents of the farming contract:

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Structure of the farming contract:

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- Centralized Farming Contract; and
- Plantation Farming Contract.

II. COMMON BREACHES OF CONTRACT FARMING



III. Dispute Settlement

1. Judicial organizations having binding decisions

- Courts of Vietnam;
- Arbitration.

2. Subjects having non-binding decisions

- Commune People's Committee;
- Farmer Union; and
- Inspection Agency.

1. Having binding decisions

a. The Court of Vietnam

- Various levels, with the Supreme People's Court, the provincial People's Court, the district People's Court;
- Each level has different jurisdiction;
- In practice, this is the most popular judicial organization parties ask once there is any dispute arises;
- Although the expenses in Court are really low, the legal proceedings may be lasted for years.

1. Having binding decisions

b. Arbitration

- The disputes resolution by arbitration is also applicable in Vietnam even though it is not common as with the cases settled by courts.
- Vietnam's arbitrators have jurisdiction over commercial disputes.
- The arbitration body which is considered the most experienced and best recognized is Vietnam International Arbitration Centre (VIAC) in conjunction with the Vietnam Chamber of Commerce & Industry (VCCI).
- The farmers often deny this kind of settlement.

1. Having binding decisions

C. Foreign Court and arbitration

- o Vietnam and the country which renders such civil judgment or decision have signed or acceded to international treaties on this matter; and
- o The judgment is not prohibited by the laws of Vietnam from being recognized and enforced.

2. Having non-binding decisions

- o Negotiation and mediation;
- o Commune People Committee, Farmer Union and Inspection Agency;
- o Short time and simple procedure;
- o The lack of experience in solving big-value-contract of relevant bodies; and
- o The non-binding characteristic.

3. Recommendation

Current negative effects

- ☐ Balance the relationship between the farmer and the traders;
- ☐ The role of Authority, Farmer Union and others;
- ☐ Rules of Court, Arbitration and other legal mechanism.

Proposal

- ☐ convert the non-binding mechanism into binding mechanism; and/or
- ☐ create a special jurisdiction body.

IV. RESULT OF DISPUTE SETTLEMENT

Compensation for the material damages/loss

Penalty

Stopping the breach behaviors and continuously carrying out the contract

Terminating the contract

Terminate all support and sponsors





KINGDOM OF CAMBODIA



Ministry of Agriculture,
Forestry and Fisheries

CONTRACT FARMING and Legal Framework in CAMBODIA

Yi Bunhak,
Chief of Agro-industrial Development Office,
Department of Agro-industry (DAI)
yihak77@gmail.com
Tel: (855) 17 59 69 16

Thailand, 26 Sept 2014

(1) Introduction



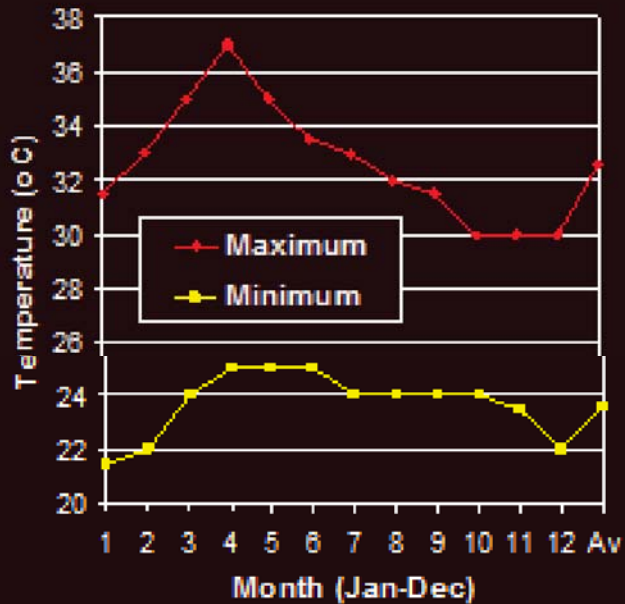
- Country area : 181.035 Km²
- Land Area : 176.520km² = 97.5%
- Agricultural Land : 31.47% (2009)
- Forest Area: 56.7% (2009)
- Water Surface : 4515 km² = 2.5%

- Population: 14,521,276 (2010)
- Population growth rate: 2,2%
- GDP per capita: 1100USD(2011)
- Labor Force:8.8 million (2010)
- Labor for agriculture: 57.6%
- Only 15% live in urban centers
- 81.2 inhabitants/km² (2011)
- 300.000-400.000 young people reach employment age each year, mainly in rural areas
- Unemployment:3.5%
- Capital : Phnom Penh

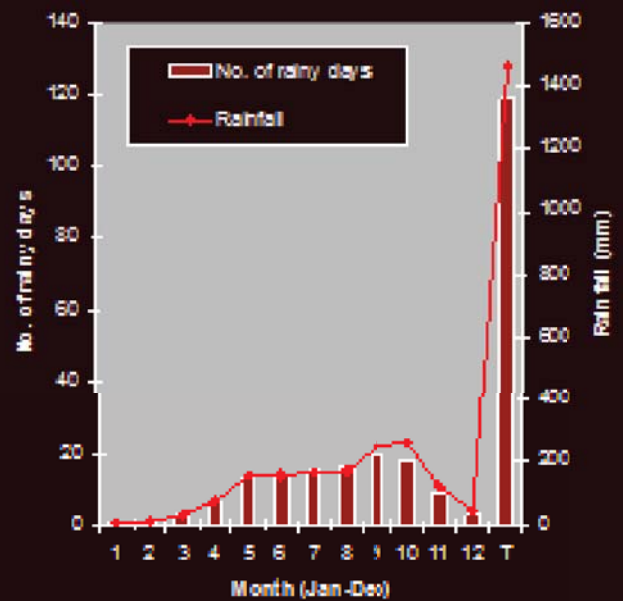
Climate



Monthly max. & min. temperature in Phnom Penh

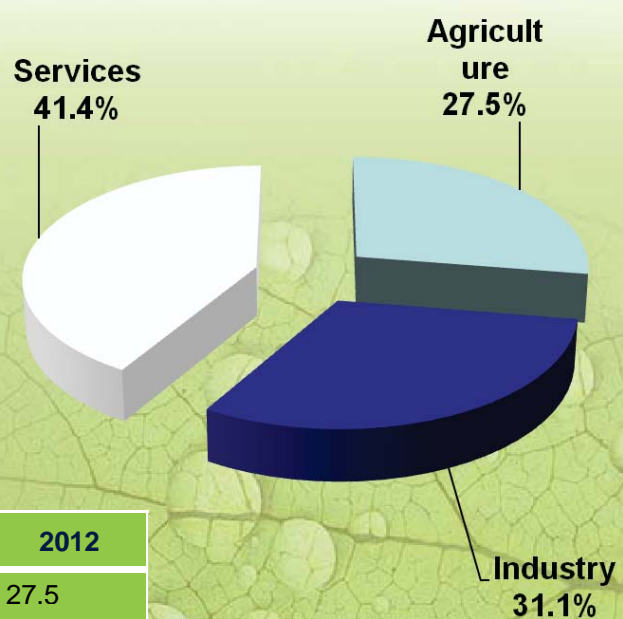


Monthly rainfall in Phnom Penh



(2) Background

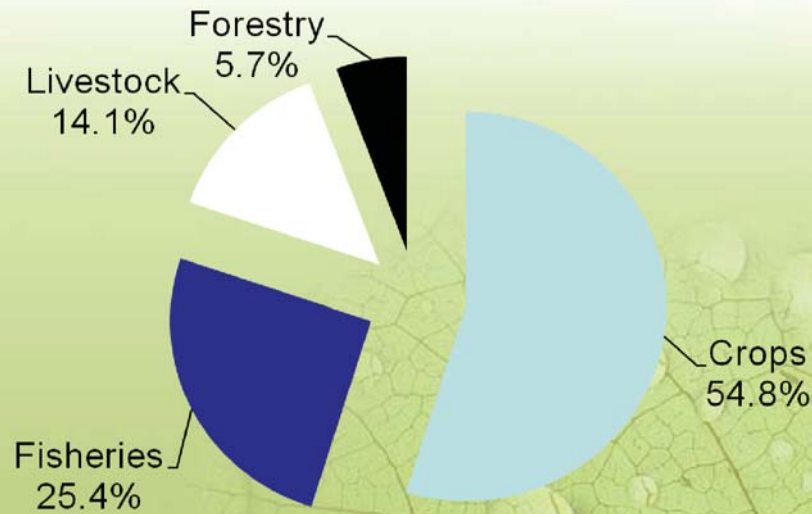
Agricultural Share in GDP (2012)



Sector	2004	2008	2012
Agriculture (%)	32.1	30.6	27.5
Industry (%)	25.4	26.2	31.1
Services(%)	42.5	43.2	41.4

(2) Background (Cont)

Composition of Sub-sector in Agriculture, 2012



	Crops	Livestock	Fisheries	Forestry
2006	50.8%	15.8%	25.9%	7.5%
2010	53.8%	12.8%	27.3%	6.1%
2012	54.8%	14.1%	25.4%	5.7

(2) Background (Cont)

Paddy Surplus (tons)



Note: 10 varieties are popularly used in Cambodia :

- Sen Pidor, IR 66, Cholasar (Early rice)
- Phkaromduol, Phkaromdeng, Phkaromeat, Phkarchansensor (Medium rice)
- Rangchey, Khar 4 , Khar 6 (Late rice)

(2) Background (Cont)

Agricultural Marketing Constraints



- Market liberalization, globalization
- 50% of farmers have land smaller 1ha
- FOs still weak in agribusiness
- Limited domestic demand
- No value addition capture (except rice)
- No access to market or market channels not known
- Lack of quality incentives and product standards
- Competition with cheap imports
- Technology and know-how constraints
- Limited on rural infrastructures
- High cost and financial constraints

7

(3) Contract Farming in Cambodia

8

(3) Contract Farming in Cambodia

CF in the Past

Government no support to be third party to facilitate such following activities below :

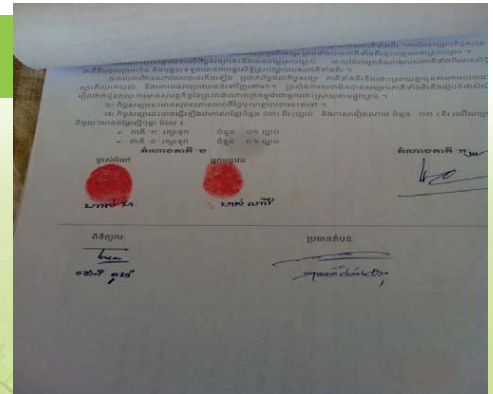
Producers ↔ Purchasers

Starting phase

- In connection
- Negotiation
- Draft contract agreement
- Technical support services
- Financial Support
- Witness by village/ commune leaders

Operation Phase

- Facilitate in conflict resolution, but by authorities, NGOs, layer, court...etc.



(3) Contract Farming in Cambodia(cont)

From year 2012

CF in the Past



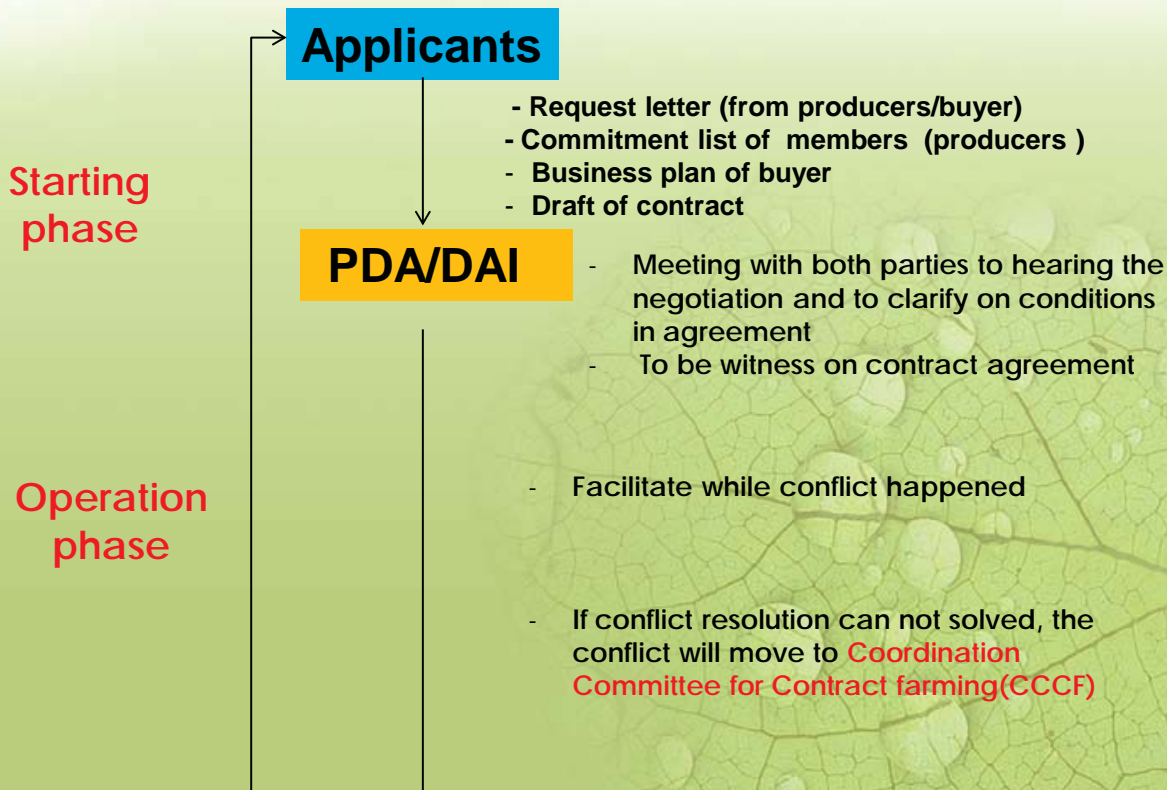
Subdecree No.36 dated Feb 2011 on Contract farming

Informal CF

Formal CF

Guideline for CF Arrangement

Follow sudecree 36



Conditions on Contracted Agreement

AGREEMENT

- (1) Subject of Contract.....
- (2) Duration of Contract.....
- (3) Right and Responsibilities of Producers.....
- (4) Right and Responsibilities of buyer.....
- (5) Harvesting and Delivery.....
- (6) Quality set ting.....
- (7) Price Setting.....
- (8) Payment Procedure.....
- (9) Natural Disasters.....
- (10) Conflict Resolution.....

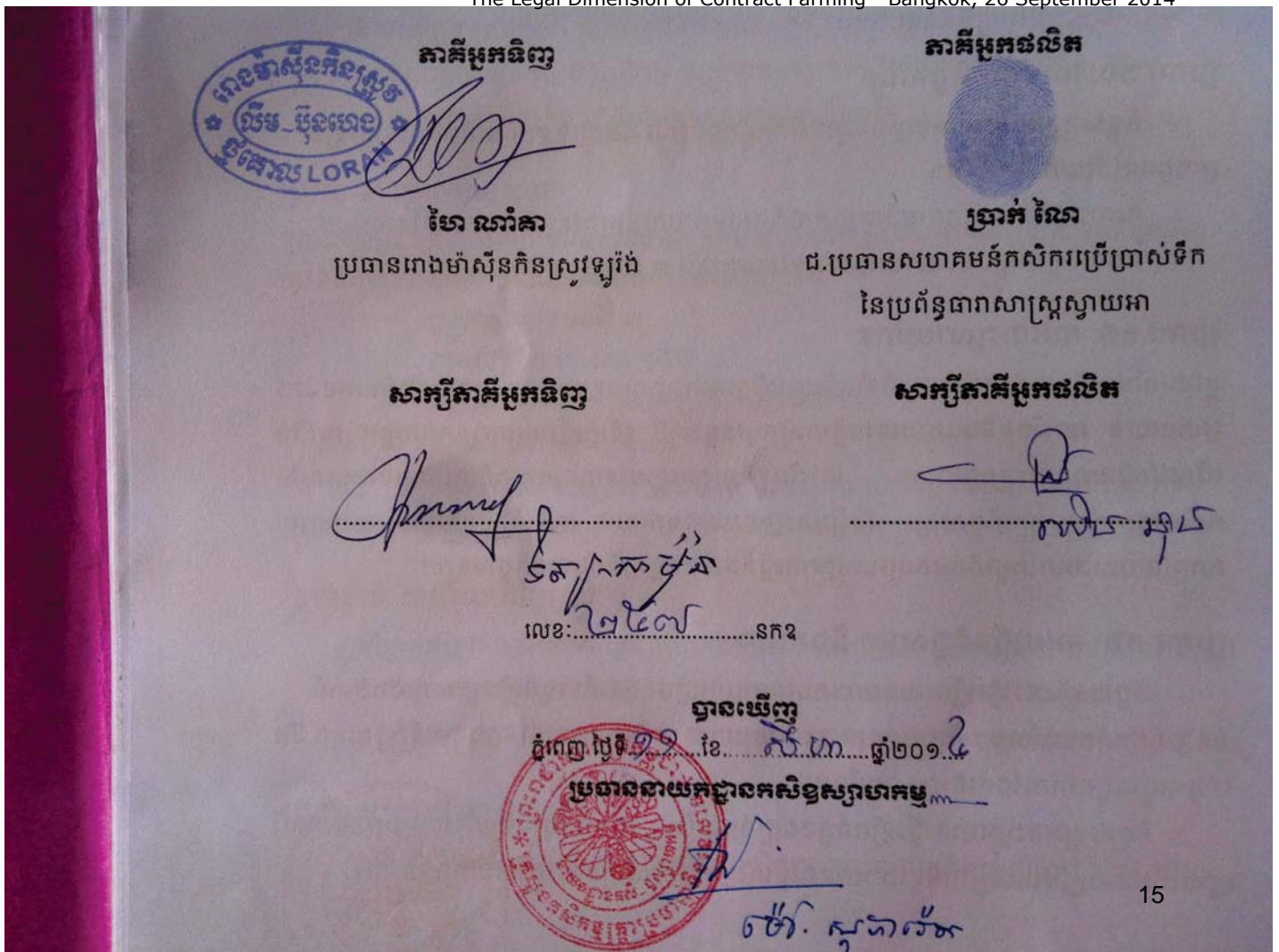
Producer Witness Buyer Witness

Recognition

PDA/DAI

Negotiation meeting





Coordination Committee for Contract Farming (CCCF)

No	Ministry	Position	Position in CCCF
1	M. Agriculture, Forestry, and Fisheries	Minister	Chairman
2	M. Inertia	Secretary of State	Vice-Chairman
3	M. Council Minister	Secretary of State	Member
4	M. Economic and Finance	Secretary of State	Member
5	M. Commerce	Secretary of State	Member
6	M. Environment	Secretary of State	Member
7	M. Land Management Urban Planning and Construction	Secretary of State	Member
8	M. Water Resource and Metrology	Secretary of State	Member
9	M. Rural Development	Secretary of State	Member
10	M. Justice	Secretary of State	Member
11	M. Public Work and Transportation	Secretary of State	Member
12	M. Industry, Mines & Energy	Secretary of State	Member
13	Council for Cambodian Development	Secretary General	Member
14	Council for Agricultural and Rural Development	Secretary General	Member
15	Cities and Provincial Municipals	Chairman	Member
16	Rural Development Bank	General Director	Member
17	Cambodia Chamber of Commerce	President	Member

Conflict Resolution Process

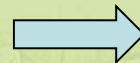
Phase 1

Conflict was solved by Both parties



Phase 2

PDA to be lead to facilitate on the conflict



Phase 3

Conflict was solved by
**Coordination
Committee for
Contract Farming
(CCCCF)**

17



Ministry of Agriculture,
Forestry and Fisheries

THANK YOU



Contact Person :

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- Mr. Yi Bunhak , Tel: (855) 17 59 69 16 , E-mail: yihak77@gmail.com

18

CLOSING REMARKS

Professor Henry Deeb Gabriel *

On behalf of UNIDROIT and particularly the Contract Farming Working Group,

I would like to thank everyone today who participated in this important consultative workshop.

It was a great personal honor to be part of these important presentations and discussions.

The number of countries and organizations represented here today is most impressive, and this truly shows the high importance given to contract farming throughout Asia, both by governments as well as farming organizations.

The presentations and discussions today will certainly inform and improve the Legal Guide to contract Farming.

Hopefully we also achieved another goal today as well by giving all of us new found knowledge and insights that we can take back with us in our own work in contract farming.

Thank you again, and I hope all of you have safe travels home.

With that, I am pleased to close today's workshop.

* Chairman of the UNIDROIT Working Group on Contract Farming; UNIDROIT Governing Council member.

**Promoting Good Contract Practices between Producers and Buyers
in Contract Farming Operations in the Asian Context**

THE LEGAL DIMENSION OF CONTRACT FARMING

**Consultation Workshop on the
UNIDROIT / FAO Legal Guide on Contract Farming**

BANGKOK, 26 September 2014
Century Park Hotel – 9 Ratchaprarop Road, Pratunam-Victory Monument

Simultaneous interpretation English/Thai/English
is provided with the kind support of the European Union



Presentation

The practice of engaging in crop or animal production based on contract farming arrangements has developed very significantly in many developing and emerging economies. Under agricultural production contracts, agricultural producers undertake to engage in production and deliver, at a future time, goods meeting designated specifications. The purchaser – typically a food processor, an exporter or a retailer – commits itself not only to acquire the product for an agreed price, but also to provide a certain level of guidance and support during the production process, typically by supplying agricultural inputs, technology, or agronomical supervision. While the success of contract farming may depend on many elements, one key element is the ability of the parties to build stable, commercially-sound and fair relationships based on clear commitments and mutual compliance. The cornerstone of the relationship is the agreement.

This workshop will focus on the legal aspects of the parties' agreement based on practical experiences and the treatment of contract farming in domestic legislation. It is addressed to a broad audience of stakeholders in contract farming relationships in the Southeast Asia region, *i.e.* producer organizations, private sector representatives, IGOs and development agencies, NGOs, public entities and the legal academic circles.

Notably, this workshop will inform the drafting of the Unidroit/FAO *Legal Guide on Contract Farming* which intends to provide soft guidance and an internationally-recognised reference with a fair and balanced approach against which contract practices and relevant public policy instruments could be assessed. The *Guide* is being prepared by the International Institute for the Unification of Private Law (UNIDROIT), together with the Food and Agriculture Organization (FAO), and the participation of the International Fund for Agricultural Development (IFAD).

At the workshop, a draft abstract of the forthcoming Guide will serve as a reference for the discussion. Participants are invited to actively take part in the workshop by sharing experience and knowledge.

PROGRAMME

8:30 – Participant registration

9:00 – 9:30 Welcome and Opening

Mr Olan Pituck
Director General, Department of Agricultural Extension
Ministry of Agriculture of Thailand

Mr Hiroyuki Konuma
Assistant Director General and Regional Representative for Asia and the Pacific
Food and Agriculture Organization of the United Nations (FAO)

Mr Benoit Thierry
Country Program Manager
International Fund for Agricultural Development (IFAD)

Mr Henry D. Gabriel
Professor of Law, School of Law, Elon University (USA)
UNIDROIT Governing Council Member
Chairman of the UNIDROIT Working Group on Contract Farming

9:30 – 10:15 Session 1 – Contract farming: An Economic and Legal Introduction

An overview of the potential of contract farming to promote more efficient agricultural supply chains and economic and social inclusion of small farmers; and an overview of the main legal issues involved in contract farming under the transactional perspective, with a presentation of the forthcoming UNIDROIT/FAO Legal Guide on Contract Farming: its scope, purpose and content

Moderator for Sessions 1 and 2

Ms Lawan Thanadsillapakul
Professor of Law, School of Law
Sukhothai Thammathirat Open University, Thailand

Contract farming and inclusive value chain development

Mr Carlos A. da Silva
Senior Agribusiness Economist
Rural Infrastructure and Agro-Industries Division (AGS)
Food and Agriculture Organization of the United Nations (FAO)

Contract farming: a legal approach. The forthcoming UNIDROIT/FAO Legal Guide on Contract Farming

Mr Henry D. Gabriel
Chairman of the UNIDROIT Working Group on Contract Farming

10:15 – 10:45**Session 2 – The Legal Framework for Producer-Buyer Relationships – Country Overview**

An overview of the diversity of approaches in the legal regime applicable to contract relations between producers and buyers, against the backdrop of the economic and social functions of contract farming. And a tentative assessment as to whether the mandatory rules and existing gap-filling methods applicable to contract farming relationships – including in case of dispute – provide adequate solutions to enhance fair terms and behaviours.

Introduction of the session and an Overview of the Legal Treatment of Contract Farming in Thailand

Ms Lawan Thanadsillapakul

Philippines

Hon. Virgilio R. de los Reyes
(Former) Vice Dean of the De La Salle University College of Law
Secretary, Department of Agrarian Reform
Quezon City, Philippines

10:45 – 11:15 Refreshments**11:15 – 12:30****Session 2 – The Legal Framework for Producer-Buyer Relationships – Country Overview (continued)****Indonesia**

Mr Paripurna P Sugarda
Professor of Law, University of Gadjah Mada Faculty of Law
Yogyakarta, Indonesia
Member of the UNIDROIT Working Group on Contract Farming

Cambodia

Mr Prasnar Yi
Lecturer of Law, Royal University of Law and Economics (RULE)
President of Henri Capitant Friends of Cambodian Law Association
Phnom Penh, Cambodia

Vietnam

Dr Dang Kim Khoi
Center for Agricultural Policy, Institute of Policy and Strategy for Agricultural
and Rural Development – IPSARD
Hanoi, Vietnam

Discussion and Conclusions

12:30 – 14:00**Lunch Provided by UNIDROIT****14:00 – 15:30****Session 3 – Contract Formation and Obligations of the Parties**

Practical Experiences Panel 1: A moderated panel, as well as the full group of participants, will share experiences, recommendations, and best practices focusing on issues related to the negotiation process, the conclusion of the contract and the definition of reciprocal contractual obligations

Moderator

Mr Benoit Thierry
Country Program Manager, Cambodia and Thailand
International Fund for Agricultural Development (IFAD)

Panelists

Mr Ubol Yoowah
Vice Chairperson, Community of Agro-Ecology Foundation – CAEF
Thailand

Mr Sok Sarang
National Team Leader of Component #3 (Contract Farming)
Support to the Commercialization of Cambodian Rice Project (SCCRP)
Cambodian Institute for Research and Rural Development - CIRD
Cambodia

Mr Jude A. Andrada
Head, Accounts Management and Development Group
National Livelihood Development Corporation
Philippines

Mr Andrew Cockburn
Sadhana Arifnusa Corporation (Sadhana)
Indonesia

Mr Souvanthong Namvong
Deputy Head of Training Section, Department of Agriculture Extension
and Cooperatives
Ministry of Agriculture and Forestry
Vientiane, Lao PDR

Discussion and Conclusions

15:30 – 16:00**Refreshments****16:00 – 17:30****Session 4 – Performance, non performance and Dispute Resolution**

Practical Experiences Panel 2: A moderated panel, as well as the full group of participants, will share experiences, recommendations, and best practices focusing on issues related to performance of parties' obligations, as well as non performance/breach – including excuses and remedies – and dispute resolution mechanisms

Moderator

Mr Ralph Houtman
Agriculture Officer (Value Chains, Marketing, Rural Finance)
FAO Regional Office for Asia and the Pacific, Bangkok
Thailand

Panelists

Mr Antonio Salvador
Legal Consultant
Asian Farmers Association (AFA)

Mr Ab Rahman Ismail
General Manager, National Farmers Organization (NAFAS)
Malaysia

Ms Mattana Gosoomp
The co-funder of Sustainable Alternative Development Association (SADA)
Thailand

Mr Tran Quoc Dat
Deputy General Director, Hiep Tai Food Company Ltd,
Vietnam

Mr Yi Bunhak
Chief of Development Agro-Industry Office/DAI
Ministry of Agriculture, Fisheries and Forestry,
Cambodia

Discussion and Conclusions**17:30 Closing of the session**

Mr Henry D. Gabriel
Chairman of the UNIDROIT Working Group on Contract Farming



UNIDROIT is an intergovernmental organisation that prepares draft harmonised rules of private law as well as softlaw guidelines and principles to assist in the modernisation of domestic legal frameworks. UNIDROIT is coauthoring the Guide and serves as primary project organizer.



FAO focuses on achieving food security for all. FAO devotes resources to contract farming by implementing development programmes, issuing publications and running a Contract Farming Resource Centre. FAO is coauthoring the Guide and has provided support through the sharing of expert knowledge and the participation of delegations of experts and providing comments and inputs on the drafts.



IFAD mobilises and deploys resources to fight rural poverty. IFAD has provided support through the sharing of expert knowledge and the participation of delegations of experts providing comments and inputs on the drafts. In addition, IFAD is providing substantial support to the preparation of the Guide through a grant to FAO (recipient)

More detailed information about this project can be found on UNIDROIT website at:
<http://www.unidroit.org/workinprogressstudies/currentstudies/contractfarming>

Check out FAO's Contract Farming Resource Centre for more information:
<http://www.fao.org/ag/ags/contract-farming/en/>

For any questions or comments regarding this project, please contact:
info@unidroit.org

The Agricultural and Food Marketing Association for Asia and the Pacific (AFMA) is an organising partner for the Workshop.



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Bangkok, 26 September 2014

LIST OF PARTICIPANTS *

STATES

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Mr Olan Pituck - Speaker

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Dr Lawan Thanadsillapakul - Speaker

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