Production Shortfalls in Grain Contracts

If you are unable to meet grain contract obligations during a production shortfall, because of adverse growing conditions, this can create a very stressful situation. However, there are steps you can take to come up with a plan that will address production shortfalls.

Determine your options

Step 1: Understand your grain contract. Grain contracts are legally enforceable agreements that bind buyers and sellers to a set of predetermined actions for delivering and selling grain. The details in these contracts vary between grain companies and the types of grain being sold. If you review and understand the commitments and obligations in your grain contract, you'll have the framework to develop a plan for a production shortfall.

Step 2: Contact the grain company. Many contracts require you to contact the grain company as soon as you think there will be a production shortfall, and there won't be enough grain to fulfill your outstanding contracts. If you do this early, you'll have time for a conversation with the grain company to see what options are available for both of you. The grain company has also made commitments to its business stakeholders on the grain it has contracted with you, so the company is in a similar situation to yours during a production shortfall.

Step 3: Weigh your options. There are a number of ways to resolve a production shortfall on grain contracts. You may need to pay the grain company the difference between your contracted price and the current market price. There may be a set monetary penalty if you don't deliver the quantity and/or quality of grain you agreed on. The grain company may also charge an administration fee to release you from the portion of the contract you aren't able to fulfill. Be sure to ask if you can roll ahead your outstanding grain contract to the next crop year. There may be room to negotiate and deliver a different type of grain to the company. The grain company may also give you some consideration if you commit to purchasing some cropping inputs from them for the next crop year. While most contracts don't have an act of God or force majeure clause, some of them may simply be cancelled if there is a crop failure and you can show documentation of a severe production shortfall.

Step 4: Consider the impact of your decision. It's important to try and maintain any goodwill between your business and grain companies to see yourself through the current crisis and to maintain your business relationships into the future. The best grain companies to deal with are the ones who want to work out an equitable solution for everyone. Grain companies that are difficult to deal with or offer one-sided solutions are poor business partners, so it's best to review your future business dealings with them.

Step 5: Consult with your legal advisor. Some solutions to production shortfalls on grain contracts are simple and straightforward and don't need consultation with your legal advisor. However, if you're uncomfortable or unsure about your options with a grain company, check with your legal advisor to review all the possible impacts on your operation.

Step 6: Implement your plan. Contact the grain company, tell them about your decision and carry out the solution.

Other considerations

Consider your relationships with grain companies. This is a stressful time, and it's understandable to be frustrated because of a production shortfall. Remember, grain companies are in a similar situation to yours, with low grain volumes and outstanding commitments. Superior grain companies will want to protect their relationships with producers as best they can. The best business partnerships are the ones where both parties can be profitable over the long-term.

Are there any set offs in your grain contract? Set offs are clauses in grain contracts that may allow the grain company to deduct any money owing from the cancellation of a grain contract from other business transactions. Examples of this include a grain company deducting grain contract cancellation fees from delivery proceeds from another class of grain, or from any credits on the crop inputs side of the business.

Are there any implications to your income tax situation or AgriStability? Check with your tax professional to see if there are any negative tax implications for you. Also, ask your tax professional if buyout costs on grain contracts can be used as eligible expenses in the AgriStability program.

Do a more detailed review of your grain contracts before you sign them. Experience managing adverse conditions can be the best teacher for improving your ability to manage, in terms of production management and business management. Rather than blaming yourself for not fully understanding what was in your grain contract, use this experience to understand why it's important to know what's in your contract and always try to understand the contract terms as clearly as possible in the future.

Contact us

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