

Department of Legislative Services
 Maryland General Assembly
 2015 Session

FISCAL AND POLICY NOTE

Senate Bill 532 (Senator Madaleno, *et al.*)

Finance and Education, Health, and
 Environmental Affairs

Farmers' Rights Act

This bill establishes requirements for livestock production contracts between contract producers and contractors, as defined in the bill. The bill also establishes specified rights for contract producers and prohibits contractors from engaging in specified practices. Contractors are also required to remove excess waste from contract operation facilities, as specified in the bill. Violators are subject to civil and criminal penalties. The Office of the Attorney General (OAG) must review production contracts for compliance with the bill's requirements and enforce the bill. The bill applies to production contracts in force on or after October 1, 2015, regardless of the production contract's date of execution.

Fiscal Summary

State Effect: General fund expenditures increase by at least \$225,700 in FY 2016 for OAG to hire three full-time assistant Attorneys General to comply with the bill's requirements, under the assumptions discussed below. Future years reflect annualization and increases in operating costs. Minimal increase in general fund revenues due to the bill's penalty provisions for those cases heard in the District Court, to the extent of enforcement.

(in dollars)	FY 2016	FY 2017	FY 2018	FY 2019	FY 2020
GF Revenue	-	-	-	-	-
GF Expenditure	\$225,700	\$289,500	\$302,900	\$317,000	\$331,700
Net Effect	(\$225,700)	(\$289,500)	(\$302,900)	(\$317,000)	(\$331,700)

Note:() = decrease; GF = general funds; FF = federal funds; SF = special funds; - = indeterminate effect

Local Effect: Minimal increase in revenues due to the bill's penalty provisions for those cases heard in the circuit courts, to the extent of enforcement. No effect on expenditures.

Small Business Effect: Meaningful.

Analysis

Bill Summary: The bill applies to production contracts that relate to the production of livestock owned by a contractor and produced by a contract producer at the contract producer's contract operation.

Definitions

The bill defines "contract operation" as a livestock facility operated in accordance with a production contract. "Contract producer" is a producer that produces livestock under a production contract. "Contractor" is a person that owns livestock that is produced by a contract producer at the contract producer's contract operation. "Livestock" means beef cattle, dairy cattle, poultry, sheep, goats, or swine. "Producer" means a person that holds an interest in a livestock facility. "Production contract" means a written agreement that specifies the terms for the production of livestock by a contract producer.

Contract Requirements

A production contract must include a clear written disclosure statement that states the nature of the material risks faced by a producer if the producer enters into the contract. The disclosure statement must include specified provisions, may be in the form of a written statement or checklist, and may be developed in cooperation with producers or producer organizations.

A production contract entered into, amended, or renewed on or after the bill's October 1, 2015 effective date must contain a cover sheet that contains specified statements and disclosures, including a statement describing, in plain language, the producer's right to cancel the contract.

All parts of a production contract, including any attachments, must be in legible type, appropriately divided into sections with captions, and written in clear and coherent language using words and grammar that are understandable by a person of average intelligence, education, and experience within the industry.

Review by OAG

A contractor must submit a production contract to OAG for review to determine whether the contract complies with the bill's requirements. OAG may decline to review a production contract because the contract's compliance with the bill is subject to pending

litigation or the contract is not subject to the bill. After reviewing a production contract, OAG must certify that the contract complies with the bill or decline to certify the contract and state the reasons why the contract fails to comply. OAG's actions in reviewing a production contract are not subject to judicial review.

The bill establishes the following factors that OAG must consider, at a minimum, in determining whether a production contract meets the requirements of the bill: (1) the simplicity of the sentence structure; (2) the extent to which commonly used and understood words are employed; (3) the extent to which esoteric legal terms are avoided; (4) the extent to which references to other sections or provisions of the contract are minimized; (5) the Flesch Reading Ease Test (a well-known standard used to evaluate the readability of documents); (6) the extent to which clear definitions are used in the text of the contract; and (7) any other factors relevant to the readability or understandability of the contract.

A production contract certified by OAG is deemed to comply with the requirements established by the bill for the format and contents of a contract, but certification does not constitute an approval of the contract's legality or legal effect. If OAG fails to respond within 30 days after a production contract is submitted for review, the contract is deemed to comply with the bill's requirements.

Producer's Right to Cancel

A producer may cancel a production contract by mailing a written cancellation notice to the contractor within three business days after the contract is executed, or before a later cancellation deadline if such a deadline is specified in the contract. A producer's right to cancel, the method by which the producer may cancel, and the deadline for canceling a production contract must be clearly disclosed in each production contract.

Void and Unenforceable Provisions

The bill establishes that the following provisions in a production contract are void and unenforceable: (1) a provision that states that information contained in the contract is confidential, except for information determined by OAG to be confidential business information; (2) a waiver of a right of a contract producer or an obligation of a contractor; and (3) a requirement that the law of another state applies.

Production Contract Lien

Under the bill, a contract producer has a lien on the contractor's livestock for the amount of any money owed to the contract producer under the production contract, including money owed for the production of livestock and for capital investments. If the money that gives rise to the lien is due and unpaid for 30 days and the contract producer is in possession

of the livestock, the contract producer may sell the livestock to which the lien attaches at public sale, after complying with specified notice requirements.

Termination of Production Contract

Generally, a contractor may not terminate, cancel, or fail to renew a production contract unless (1) the contractor has given the contract producer written notice of the contractor's intention to terminate, cancel, or not renew at least 90 days before the effective date of the termination, cancellation, or nonrenewal and (2) the contract producer has been paid any money owed under the contract and reimbursed for damages incurred due to the termination, cancellation, or failure to renew.

If a contract producer materially breaches a production contract, the contractor must give notice that states the alleged causes of the breach at least 45 days before the effective date of the termination, cancellation, or nonrenewal, and give the contract producer 30 days to remedy the breach. A contractor is not required to give notice or an opportunity to remedy an alleged breach if the basis for the termination, cancellation, or nonrenewal is (1) a voluntary abandonment of the contractual relationship by the contract producer or (2) the conviction of the contract producer of an offense of fraud or theft committed against the contractor.

Except as otherwise specified in the bill, if a contractor terminates, cancels, or fails to renew a production contract, the contractor must pay the contract producer the greater of (1) the value of the remaining useful life of the structures, machinery, or equipment used in the contract operation or (2) the balance left on any loan obtained by the contract producer to build or improve a structure or to purchase the machinery or equipment used in the contract operation.

Rights of Contract Producers

The bill establishes rights of a contract producer, including:

- the right to enter into a membership agreement or marketing contract with an association of producers, a processor, or another producer, and the right to exercise contractual rights under a membership agreement or marketing contract;
- the right to lawfully provide statements or information, including to the U.S. Secretary of Agriculture or to a law enforcement agency, regarding alleged improper actions or violations of law by a contractor or processor, unless the statements or information are determined to be libelous or slanderous;

- the right to communicate freely with any other person, including members of the public, elected officials, or the press, regarding the contract producer's experience as a contract producer, except for confidential business information; and
- the right to refuse to retain all or part of the waste, including poultry litter, generated at the contract operation by the production of livestock owned by a contractor.

Additionally, a contract producer must notify the contractor in writing within five days after the contractor's removal of livestock from the contract operation of the amount of waste, if any, the producer wishes to retain. Any waste the contract producer does not wish to retain is deemed to be excess waste, and must be removed by the contractor, at no cost to the contract producer, from the contract operation within 30 days after notification by the contract producer.

Prohibited Contractor Practices

A contractor may not engage in or allow an employee or agent to engage in specified practices in connection with the terms of a production contract or its execution, including:

- taking any action to coerce, intimidate, disadvantage, retaliate against, or discriminate against a contract producer, as specified, because the contract producer exercises or attempts to exercise any right;
- providing false information to a contract producer, as specified;
- refusing to provide to a contract producer, on request, the statistical information and data used to determine compensation paid to the contract producer under a production contract, including feed conversion rates, feed analyses, origination, and breeder history;
- refusing to allow a contract producer or the contract producer's designated representative to observe, by actual observation at the time of weighing, the weights and measures used to determine the contract producer's compensation under a production contract;
- using the performance of any other contract producer to determine the compensation of a contract producer under a production contract or as the basis for the termination, cancellation, or renewal of a production contract; and

- requiring a contract producer to make new or additional capital investments that are unnecessary for the proper functioning of the contract operation or the health, safety, and welfare of the livestock or the public, except under specified circumstances.

Mediation

A production contract must contain language authorizing the resolution of disputes concerning the contract by mediation. Both parties to a production contract must agree to mediation before mediation may occur. Any decision made in mediation must be nonbinding on the parties and does not prevent any party from seeking any other legal remedy available under the bill.

Enforcement and Penalties

A contractor that engages in a prohibited practice is (1) subject to a civil penalty of up to \$50,000 per violation and (2) guilty of a misdemeanor and subject to a fine of up to \$25,000.

In enforcing the bill, OAG may (1) seek an injunction to restrain a contractor from engaging in prohibited conduct or practices or to require a contractor to comply with a provision of the bill; (2) obtain a subpoena for the production of documents; (3) bring an action for civil penalties; and (4) bring a criminal prosecution.

In addition, a contract producer that suffers damages because of a contractor's violation of the bill may bring an action to obtain appropriate legal and equitable relief, including damages. If a contract producer is the prevailing party in a civil action against a contractor, the court must award the contract producer reasonable attorney's fees and other litigation expenses.

Current Law/Background: State law does not address contracts between livestock owners and producers. However, State law does regulate several other types of commercial contracts and relationships, including equipment dealer contracts, contracts for the distribution and sale of commercial goods, sales of business opportunities and franchises, and the relationship of vehicle manufacturers and dealers.

The federal Food, Conservation, and Energy Act of 2008 (also referred to as the 2008 "Farm Bill") contained several provisions dealing with production contracts, including provisions relating to:

- ***The right of poultry growers and swine producers to cancel contracts.*** The law requires that growers and producers have at least three days from the date of contract execution to cancel. In addition, contracts must clearly disclose the cancellation rights of producers, including the method and deadline for cancellation.
- ***A requirement that production contracts state whether poultry growers or swine producers would be required to make additional large capital investments during the life of the contract.*** Specifically, if the contract requires an additional investment, the farm bill requires that the first page of a contract include such a statement.
- ***Arbitration of disputes.*** If a livestock or poultry contract contains an arbitration clause for resolving disputes, then the grower or producer must have the option to decline arbitration. Contracts must clearly disclose the right of a producer or grower to decline the arbitration provision. The law also allows producers and growers to opt for arbitration even after declining the arbitration provision at the time of contract execution, if both sides agree in writing to take a dispute to an arbitrator.

The Farm Bill required the U.S. Department of Agriculture (USDA) to propose rules to implement these provisions. According to a Congressional Research Service report, USDA's 2010 proposed rule included provisions relating to unfair discriminatory and deceptive practices and provided examples of practices by meat packers and poultry dealers that would be considered unfair practices under federal law, including (1) retaliatory actions, such as coercion or intimidation, in response to a lawful action by a producer or grower; (2) refusal to provide statistical data used to determine contract payments; (3) actions to limit producers' or growers' legal rights; (4) terminating a production contract based only on allegations of misconduct by a producer or grower; and (5) practices that are fraudulent or likely to mislead a producer or grower. However, these provisions were not included in the final rule due to restrictive provisions contained in laws governing subsequent congressional appropriations. USDA issued the final rule on livestock and poultry marketing practices on December 9, 2011, which did include provisions addressing suspension of the delivery of birds, additional capital investment, remedy for breach of contract, and arbitration.

According to the Maryland Department of Agriculture (MDA), five companies contract with farmers to raise broilers in Maryland; one for turkeys; and a small but unknown number for hogs, heifers, and eggs. Based on a 2012 census conducted by USDA, Maryland has 49 farms producing heifer cows under contract, 683 growing broiler chickens, 8 for laying hens, 2 for pullets, 6 for hogs, and 3 for turkeys. Broiler production

accounts for nearly 40% of all farm receipts in Maryland, making it the largest agricultural enterprise in the State.

State Expenditures: General fund expenditures increase by at least \$225,749 in fiscal 2016, which accounts for the bill's October 1, 2015 effective date. This estimate reflects the cost for OAG to hire three full-time assistant Attorneys General to review contracts for compliance with the bill's requirements and to enforce the bill. It includes salaries, fringe benefits, one-time start-up costs, and ongoing operating expenses. The bill requires all contractors doing business in the State to submit contracts for review to OAG; OAG must determine whether the contracts meet the bill's minimum requirements and certify, or decline to certify, the contracts accordingly. OAG must also enforce the bill by bringing civil and/or criminal action against violators.

The bill applies to all contracts in force on or after October 1, 2015, regardless of the date of execution; therefore, OAG would likely have to review a large number of the contracts currently in place, including contracts at the 683 farms growing broiler chickens in the State. This estimate assumes each such contract is reviewed annually and only one contract per farm is reviewed.

Positions	3
Salary and Fringe Benefits	\$ 211,578
Operating Expenses	<u>14,171</u>
Total FY 2016 State Expenditures	\$225,749

Future year expenditures reflect full salaries with annual increases and employee turnover as well as annual increases in ongoing operating expenses.

Depending on the volume and complexity of contracts actually received, OAG may require additional staff beyond what is included in this estimate. For example, if contract modifications must also be reviewed or significantly more contracts or agreements are executed with each farm in a given year, significantly more staff is needed to review the contracts.

Conversely, if the contracts are for longer terms and/or the requirement for review is interpreted to apply to the contract *form* rather than each contract executed, fewer resources are needed. Regardless, under this scenario, OAG would need at least one additional assistant Attorney General and contractual assistance to handle the initial influx of contracts for review.

The Judiciary advises that courts may incur expenses related to the enforcement of lien actions under the bill, and that there may be an increase in both civil and criminal filings as a result of the bill's enforcement provisions; however, the Judiciary was unable to

estimate the extent of this impact. The Department of Legislative Services assumes that any increase on the Judiciary's workload can be handled with existing resources.

The Judiciary also advises that the bill's provisions relating to mediation may impact the Maryland Mediation and Conflict Resolution Office (MACRO) and that, although MACRO itself does not offer mediation, it does provide mediation referral services and would likely refer any action arising under the bill to MDA's Conflict Resolution Service. Although the number of requests anticipated for such services cannot be reliably estimated at this time, since mediation remains only an option to which both parties of a conflict must consent, the Department of Legislative Services assumes such services can be provided with existing resources.

Small Business Effect: MDA advises that most of the companies (*e.g.*, contractors) that contract with growers (*e.g.*, contract producers) are not small businesses, although this may not be true for contractors of "replacement heifers." However, all of the contract producers in the State are believed to be small businesses.

MDA additionally advises that, although the bill is likely intended to benefit and protect contract producers, the bill may have negative long-term effects on contract growing opportunities in the State; contractors may seek to relocate production to states that do not have the bill's requirements, or may shift any increased costs to contract producers through reduced compensation.

Additional Information

Prior Introductions: None.

Cross File: HB 1019 (Delegate Fraser-Hidalgo, *et al.*) - Environment and Transportation.

Information Source(s): Office of the Attorney General, Maryland Department of Agriculture, Judiciary (Administrative Office of the Courts), Congressional Research Service, Department of Legislative Services

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