



## Agricultural Contracting

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Contracts are part of everyday life, but are especially important to individuals who are engaged in business. A contract is a legal document that represents an agreement between two or more parties and involves legally enforceable commitments or promises to do or not do something. It is important to understand that a contract is more than just a promise – it is a legally enforceable promise. This means the court can step in and enforce an agreement reached between parties. People enter into contracts almost every day and never realize it. Ordering food at a restaurant, buying supplies at a feed store, and renting land from a neighbor are some examples of the use of contracts that both producers and the general public enter into on a daily basis. While contracts are entered into and fulfilled every day, the contracts that we often think about are those that are not completed and the consequences that flow from it. As a result, it is important to look at the basics of what makes a contract and what remedies may be applied if a contract is “breached,” or broken.

### Elements of a Contract

A legally binding contract consists of five separate “elements,” or requirements. If even one of the elements is missing then no contract has been formed. The requirements are the bare essentials needed to form a contract, but contracts can and often do include many other issues. The first element is that all parties must have the mental capacity to enter into a contract. Many times this element is at issue when trying to form a contract with a minor (anyone under the age of eighteen) or with someone suffering from some form of mental illness or incapacitation. The second element involves the subject of the contract. It requires that all parties have a general idea of the purpose of the agreement. For example, assume that Allen wants to buy a tractor from Benjamin. However, Benjamin thinks that Allen is interested in purchasing a truck. As a result, a contract cannot be formed, because the parties do not agree on the subject matter. Elements three and four go hand in hand. There must be an offer to enter into a contract and an acceptance of that offer. The offer and the acceptance must match up exactly in order for a contract to be created. For example, if Allen offers to buy a tractor for \$5000 while Benjamin says he will sell for \$6000, then no contract has been formed. Instead, it forms only when the two parties agree on all of the material terms. The final required element is consideration. Consideration is defined as “the bargained exchange of something of value.” In other words, consideration is the “promise” part of the contract- it is what one party promises to do or exchange in return for the promised action from the other party. Further, consideration can take

many forms, such as money, physical objects, services, or promised actions. While these five elements are required to form a binding contract, many other important factors come in to play when making a contract.

### Written vs. Verbal Contracts

Whether it is ordering from a fast food restaurant or buying supplies at a store, many of our daily activities actually involve verbal contracts. Generally speaking, verbal contracts are as valid as written contracts; however proof that the contract exists may be difficult to show. For some contracts, the law requires that they be in writing, including many contracts that agricultural producers are likely to enter into.

In Arkansas, a law called the “Statute of Frauds” requires that certain contracts be in writing and signed by the party that is being accused of breaching the contract.<sup>1</sup> The idea behind it is that a contract is not enforceable unless there is evidence that a contract existed, and the best evidence of that is a written contract containing the terms that both parties agreed to. Contracts covered by the Statute of Frauds must also identify the parties and the essential terms and obligations of the agreement. Further, changes or additions to the contract must also be in writing and signed as well.

Here are a few of the contracts typically used in agriculture that must be in writing according to the statute of frauds.

- Contracts that cannot be performed within one year (such as leases that last for more than one year)
- Real estate sales
- The sale of goods over \$500<sup>2</sup>
- Agreeing to become a “surety,” or becoming responsible for another’s obligation or debt

However, even if the Statute of Frauds does not require that a contract be in writing, it is always a good business practice to have all contracts in writing. Simple contracts such as ordering food at a restaurant do not have enough critical details to warrant the writing of a contract, but many contracts that producers enter into cover more topics besides the five required elements. Written contracts become essential as the agreement becomes more complex.

### Breach of Contract

When you agree to a contract, you promise to fulfill your specific part of the contract. Failure to do so is a breach of the contract, and the other parties to the contract can sue for legal remedies. Typically courts will hear cases regarding contract breaches and disputes; but it is becoming more common to include a contract provision allowing a mediator or arbitrator decide the issue. One example of this approach can be found in crop insurance contracts. If a dispute arises under a crop insurance agreement then the parties are required to submit to arbitration instead of taking the matter in front of a court.

The consequences resulting from a breach of contract also depend on the language of the contract. However, many times a contract is silent about the results that will occur in the event

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<sup>1</sup> A.C.A. § 4-59-101

<sup>2</sup> This factsheet does not discuss the Uniform Commercial Code, which also addresses the sale of goods

of a breach. In these cases the damages, or consequences, of the breach will be assigned by the court or arbitrator. The general rule for broken contracts is that the damages should compensate the party that was damaged by whatever amount that they would have made had the contract been completed successfully.

**Example:** Smith and Jones enter into a contract for Smith to sell Jones a bag of seed for \$300. Jones planned on selling that seed to a third party for \$1,000. Smith refuses to deliver the seed. In this case, Jones would be entitled to recover \$700 because that was what he was expecting to make on the contract with Smith.

The goal is to make the damaged party “whole,” not to punish the party that committed the breach. While it is possible that a breach by one party has terminated the contract, that is not always the case. Depending on the severity of the breach it may also be possible the contract itself has to be terminated such as in the example above. However, many contracts today are complicated legal documents that require multiple actions from both parties. Just because one party breaches the contract does not mean that the contract is void, or that the injured party does not have to complete performance of the contract. The best course of action in this situation is to contact a licensed attorney to help determine your options.

Other than monetary damages, the court may also order specific performance of the contract. Specific performance occurs when the court requires one party to complete their contractual obligations. This remedy is available primarily in situations where money damages are considered to be an inadequate remedy. An agricultural example of this type of judgment might be found in a contract to sell land. If the seller of the land refuses to follow through with the contract, no amount of money will put the buyer into the situation that they would have been in if the contract had been fulfilled. This is because that piece of land is unique and no other piece of property in the world is exactly like the one in the contract. Because there is no other piece of property available that is exactly like the one in question a judge may require specific performance and force the seller to complete the contract.

### Tips for Contracting

Always read a contract carefully, before it is signed. The language in the written contract will override any verbal agreement between the parties. Contracts are extremely flexible before they are signed. Just because you receive a contract that has already been drafted does not mean that it cannot be changed before it is signed. Many contracts that are written by one party often favor that party greatly, which makes it important to carefully read it over before signing. If you wish to amend the contract or include any verbal agreements between the parties, those changes must be in writing. Changing the writing can be done by marking through the section that the parties wish to amend and then writing in the changes with both parties initialing next to the change to acknowledge it.

This flexibility makes contracts useful in the real world because parties to the contract can essentially agree to do almost anything, so long as it is legal. All five of the elements must be present in order for a valid, enforceable contract to form; however many other issues may also be addressed in the contract. These issues may include such things as whether the contract may

be cancelled, what happens in case of contract breach, specifics about contract performance and what the possible results are if an unforeseen event makes performing the contract impossible, among others. Because the details are so critical when dealing with contracts it is important to put time and effort into writing and reviewing the contract before it is entered into.