

Grain Contracts

Managing Counterparty Risk

Irrespective of where you operate in the grain supply chain, your grain contracts confer certain rights and responsibilities. A key responsibility for a seller is to make delivery against the contract and a key right is to receive payment for grain delivered against the contract when due and payable as defined in the contract.

A key right for a buyer is to receive grain against a contract and a key responsibility is to make payment for grain delivered against the contract when due and payable as defined in the contract. However, parties to a contract can never be guaranteed that their rights or responsibilities will be upheld on all occasions.

This fact sheet will highlight some of the major actions that a party can use to assist in determining a method to reduce risk when selling grain. This list is not exhaustive and not all actions can or will apply in every situation.

Irrespective of the size of your organisation, before you sell any grain, it is fundamental to consider the risk and potential impact to your business if the buyer fails to pay for the grain.

It is important to establish some rules about how to determine who to sell to, how much to sell in a contract before payment is received and what actions you will take if payment is late.

GTA is often approached when an organisation becomes insolvent and the argument is proposed that there should some type of guarantee payment process implemented as parties do not have the time or experience to conduct their own due diligence.

Grain contracts quite often have a face value of hundreds of thousands of dollars. Ask yourself the question if you would be willing to lend that amount of money to the

buyer in question. If you consider the trade in this light it will ensure that you scrutinise the counterparty and the contract that binds the parties.

Lastly, grain contracting is a voluntary undertaking. There are no legislative impediments and any grain industry participant is free to contract with whoever they deem fit. It's the industry and type of economy we live in.

CONDUCTING DUE DILLIGENCE

It is important to conduct thorough due diligence before committing to a contract. The following notes are provided as an aid only. Specialist information pertinent to your commercial environment should be sourced from professional accountants and / or solicitors. Below is a checklist (in no particular order)

Is the organisation a member of GTA?

Whilst membership is not a guarantee of future performance, it is a good starting point as it demonstrates organisations that are prepared to adhere to the requirements of the Australian Grain Industry Code of Practice. Check out GTA members on the website www.graintrade.or.au



Do you know anything about the organisation?

Do they have a strong payment record? Is it possible to find out anything about their financial situation? Are they organised?

Peer / adviser / agent review

Check the organisation out with your peers or a grain marketing adviser/agent who is prepared to give you an impartial opinion. Understanding how an organisation has paid other creditors may provide insight into potential payment behavior.

Australian Securities & Investment Commission report

Do a check with the Australian Securities & Investment Commission to determine the legal status of the organisation. This search will reveal details such as:

- A listing of the directors and office holders
- Address of the Registered Office
- When the organisation was established
- Any changes to company structure, i.e. resignation and/ or appointment of Directors

Confidential report from your bank

Ask your bank for a confidential report on your counterparty. Fees will apply.

Credit insurance

Consider credit insurance to cover bad and doubtful debts.

Credit report from a commercial provider

Once you have satisfied yourself regarding the structure and status of the organisation a credit report should be obtained. The credit report will enable you to see if there are any defaults registered against the business you have selected. There are a number of organisations that provide a credit report.

Writing a Contract

The price is suitable and you have conducted a due diligence that satisfies the credit worthiness of your counterparty. The next step is to commit to the contract.

The vast majority of trade negotiations occur via telephone communication directly with counterparties or through specialist advisers, agents or brokers. A trade is concluded when one party agrees to sell (the offer) and the other party agrees to purchase (the acceptance or bid) goods for an agreed value (the financial consideration). This agreement is otherwise known as the contract and has been negotiated on a telephone call.

Ensure the negotiations cover all aspects of the terms and conditions that could impact the trade. If required, request a copy of a contract proforma prior to agreement to ensure you are across the issues to be negotiated.

Reconfirm all aspects of the contract negotiations at the conclusion of the telephone conversation.

Check that the contract confirmations accurately reflect the contract and revert to your counterparty with any amendments/changes IMMEDIATELY.

Keep on top of payments

If payments are late, make sure action is taken or, at the very minimum do not sell more grain to that buyer until payment is made.

If you are using an Agent or Broker notify them if payment is late so they can pass this information onto other sellers.

Storage Agreement

A storage provider could also be a counterparty. Issues can arise where there is no storage agreement, the grain is co-mingled and the storage provider becomes insolvent. GTA has developed a Storage & Handling Agreement which references the ability to claim title in co-mingled grain.

Key points

- Irrespective of where you are in the grain supply chain it is incumbent on you to understand the risks associated with entering into a contract
- Conduct your due diligence. Know who your counterparty is so you can assess the level of risk in dealing with them
- Take the time to fully understand the terms and conditions of the contract
- Keep on top of payments. If they are late, do not sell more grain to that buyer until payment is made

Personal Property Securities Register

Register your interest in the contracted grain on the Personal Property & Securities Register. If you are unsure how this applies seek professional advice.

CONCLUSION

- Entering into a grain contract is not an action to be taken lightly. Parties quite often focus solely on price and give insufficient regard to the contract or who the counterparty is. In many cases these issues are more important.
- Consider the dollar value of risk to the buyer in question.
- You have a responsibility to yourself and your organisation to conduct a due diligence of your counterparty.
- During contract negotiations, cover all the relevant points listed on the contract. Ask for a copy of a contract proforma to ensure you are across the issues to be negotiated.
- Re-confirm the contract details at the end of the telephone conversation to ensure there is

agreement by both parties that all details and the corresponding obligations are fully understood.

- Forward a Contract Confirmation to your counterparty.
- Check Contract Confirmations thoroughly.
- Where there is a discrepancy between a Confirmation and the original contract, contact your counterparty immediately to clarify the exact terms and conditions. If required amend the confirmation.
- If there is an amendment to the contract, ensure that a written confirmation of any changes or amendment is exchanged between the parties.
- Monitor payments and take action if they are late including notifying your agent or broker.

FURTHER INFORMATION

Visit the GTA website for further information including our publication *A Guide to Taking Out Contracts to Supply Grain*, industry briefing papers, GTA contract and agreement proforma's and professional development courses and training available.