

## FACT SHEET

Series No. 003

Date of Issue: 14/07/2014 – Updated July 2019



# Grain Contracts

## Managing Counterparty Risk

This fact sheet highlights some of the major actions that a party may elect to employ 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.

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.

Due diligence of your counterparty is a critical step. Grain contracts quite often have a face value of hundreds of thousands of dollars and warrant establishing business processes to gauge the ability of the counterparty to meet contractual payment obligations.

Scrutiny of the counterparty and the contract used to bind the parties is a necessary step.

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.

### CONDUCTING DUE DILIGENCE

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

#### Is the counterparty a member of GTA?

Whilst membership is not a guarantee of future performance, it is a good starting point as it



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; and
- 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 may apply.

#### Credit report from a commercial provider

Once you have satisfied yourself regarding the structure and status of the counterparty a credit report should be obtained. The credit report provide access to information as to any defaults registered against the counterparty. There are a number of organisations that provide credit reports.

#### Writing a Contract

If the contract terms are suitable and you have conducted a due diligence that satisfies the credit worthiness of your counterparty. Parties can place too strong a focus on price and give insufficient regard to the contract terms and conditions or the financial capability of the counterparty. In many cases these issues can be more important.

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 <http://www.graintrade.org.au/membership>

#### Do you know anything about the counterparty?

Do they have a strong payment record? Is it possible to find out anything about their financial situation? Do they appear professional in their dealings with you and are they organised?

#### Peer / adviser / agent review

Discuss the counterparty 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

The next step is to commit to the contract.

Most 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 understand the terms and conditions open for negotiation.

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

Upon receipt of the contract confirmation check it accurately reflects the agreed terms and conditions 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.

You may wish to inform your peers and your Agent or Broker if payment is late so they can consider appropriate action.

#### Storage Agreement

A storage provider storing grain on your behalf could also be a counterparty. Issues can arise where there is no appropriate 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.

#### 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.

#### GTA TRAINING AND DEVELOPMENT

GTA offers unique grain industry specific [Training and Development](#) programs to increase knowledge and skills across the

## 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

grain value chain. These courses can be taken individually or combined into the Diploma in Grain Management.

There is a specific course Trade Rules and Contracts (DGMRUL501A) that will help all participants in the supply chain to better understand the risks involved in grain marketing.

Growers are encouraged to attend and participate in these programs. Just as it makes sense to undertake training and development in growing grain, it also makes sense to undertake training in grain marketing and risk management to minimise your business risk and improve profitability.

#### CONCLUSION

- Entering into a grain contract requires careful consideration. 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 at 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 terms and conditions 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.
- Ensure there is a commitment to forward a Contract Confirmation as soon as practicable.
- Check Contract Confirmations thoroughly and immediately upon receipt.
- 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 any term and condition of the contract, ensure 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.
- Improve your knowledge and understanding through training and development programs.