



An overview of contract farming: Legal issues and challenges

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Abstract

Recently, the Ministry of Agriculture released a draft Model Contract Farming Act, 2018. The draft Model Act seeks to create a regulatory and policy framework for contract farming. Based on this draft Model Act, legislatures of states can enact a law on contract farming as contracts fall under the Concurrent List of the Constitution. In this context, we discuss contract farming, issues related to it, and progress so far.

Keywords: contract farming, regulatory, agricultural produce marketing committee (APMC), producer, buyer, farmer

Introduction

What is contract farming?

Under contract farming, agricultural production (including livestock and poultry) can be carried out based on a pre-harvest agreement between buyers (such as food processing units and exporters), and producers (farmers or farmer organisations). The producer can sell the agricultural produce at a specific price in the future to the buyer as per the agreement. Under contract farming, the producer can reduce the risk of fluctuating market price and demand. The buyer can reduce the risk of non-availability of quality produce.

Under the draft Model Act, the producer can get support from the buyer for improving production through inputs (such as technology, pre-harvest and post-harvest infrastructure) as per the agreement. However, the buyer cannot raise a permanent structure on the producer's land. Rights or title ownership of the producer's land cannot be transferred to the buyer.

What is the existing regulatory structure?

Currently, contract farming requires registration with the Agricultural Produce Marketing Committee (APMC) in few states. This means that contractual agreements are recorded with the APMCs which can also resolve disputes arising out of these contracts. Further, market fees and levies are paid to the APMC to undertake contract farming. The Model APMC Act, 2003 provided for contract farming and was released to the states for them to use this as reference while enacting their respective laws. Consequently, 20 states have amended their APMC Acts to provide for contract farming, while Punjab has a separate law on contract farming.

What are the issues with the current structure, and how does the draft Model Act seek to address them?

Over the years, expert bodies have identified issues related to the implementation of contract farming. These include: (i) role of APMCs which are designated as an authority for registration and dispute settlement in most states, (ii) provisions of stockholding limits on produce under contract farming, and (iii) poor publicity of contract farming among the farmers about its benefits.

What are the risks and benefits the farmer faces in contract farming?

There are different types of contract farming, and each type of contract farming will have its own set of pros and cons.

1. One is simple procurement;
2. In the second, the buyer provides some inputs and takes the crop according to the terms and conditions of the contract; and
3. In the third, the buyer provides inputs and planting schedules and is more involved in the agricultural process. The last one carries the most liability for the company.

The pros are the high yields and fixed prices. The cons, however, are there as both production risk and market risk. Production costs in contract farming are higher as the standard expected is higher. No company offers protection for crop failure. No crop insurance is given and thus production risk is not covered most of the time. As said earlier, many companies take advantage of the clauses in the contract in case the harvest does not meet their requirement; they tend to buy it at a lower price or reject it altogether. Thus, market risk is also not covered fully, especially when the contract prices are based on market prices, as we know that the market prices vary substantially during the season or even during the day. If your contract document is not fair, how can your practice be fair?

Can corporate farming be a reality in India?

- Legally, corporate farming cannot exist in India.
- A non-farming entity is not allowed to own land.
- The Land Ceiling Act does not permit it.
- It has not been viable most of the time.
- There have been some companies that have attempted to lease land and cultivate crops but have not met with as great a reward as expected.
- Some States have leased out so-called wastelands to some companies for corporate farming but owing to local opposition, this has stopped now.

Contract farming can help curb inflation: RBI

The Reserve Bank of India (RBI) wants the government to facilitate contract farming in India and to exempt fruits and vegetables from agri procurement laws to improve food productivity. The central bank has also called for better supply chain logistics by setting up cold chains and processing facilities to reduce wastage.

Highlighting data that show rising incomes affecting consumption patterns, Deepak Mohanty, executive director at RBI, said that increased consumption of proteins and vegetables was one of the factors driving up costs of these items. Mohanty was delivering the annual Lalit Doshi Memorial Lecture at St Xavier's College here on Monday.

"Another factor is the cost of cultivation. The dominant part of the cost of cultivation is labour. This is particularly so in our set-up with the preponderance of small holdings, which are less amenable to mechanization. There are several explanations why rural wages have increased. One explanation is that socially inclusive public policy such as Mahatma Gandhi National Rural Employment Guarantee Act (MGNREGA) has set a floor to rural wages and increased the bargaining power of the work force," said Mohanty, adding that even after factoring inflation real wages have grown.

Role of Agricultural Produce Marketing Committees/Marketing Boards

The NITI Aayog observed that market fees and other levies are paid to the APMC for contract framing when no services such as market facilities and infrastructure are rendered by them. In this context, the Committee of State Ministers on Agricultural Reforms recommended that contract farming should be out of the ambit of APMCs. Instead, an independent regulatory authority must be brought in to disengage contract farming stakeholders from the existing APMCs.

In this regard, as per the draft Model Act, contract farming will be outside the ambit of the state APMCs. This implies that buyers need not pay market fee and commission charges to these APMCs to undertake contract farming. Further, the draft Model Act provides for establishing a state-level Contract Farming (Promotion and Facilitation) Authority to ensure implementation of the draft Model Act. Functions of the Authority include (i) levying and collecting facilitation fees, (ii) disposing appeals related to disputes under the draft Model Act, and (iii) publicising contract farming. Further, the sale and purchase of contracted produce is out of the ambit of regulation of the respective state/UT Agricultural Marketing Act.

Registration and agreement recording

The Model APMC Act, 2003 released to the states provides for the registration of contract farming agreements by an APMC. This was done to safeguard the interests of the producer and the buyer through legal support, including dispute resolution. The procedures for registration and recording of agreements vary across states. Currently, registration for contract farming has been provided with the APMC in few states, and with a state-level nodal agency in others. Further, market fee on purchases under contract agreements is completely exempted in few states and partially exempted in others. The Committee of State Ministers on

Agricultural Reforms recommended that instead of a APMC, district-level authorities can be set-up for registration of contract farming agreements. Further, any registering authority should verify the details such as the financial status of the buyer.

Under the draft Model Act, every agreement should be registered with a Registering and Agreement Recording Committee, which will be set up consisting of officials from departments such as agriculture, animal husbandry, marketing, and rural development. Such a Committee can be set up at the district, taluka or block levels.

Disputes between the producer and the buyer

The Ministry of Agriculture and Farmers Welfare observed certain risks related to upholding the contract farming agreement. For example, producers may sell their produce to a buyer other than the one with whom they hold a contract. On the other side, a buyer may fail to buy products at the agreed prices or in the agreed quantities, or arbitrarily downgrade produce quality. The Committee of State Ministers on Agricultural Reforms recommended that dispute redressal mechanism should be at block, district or regional-level state authorities and not with an APMC.

Under the draft Model Act, in case of disputes between a producer and a buyer, they can: (i) reach a mutually acceptable solution through negotiation or conciliation, (ii) refer the dispute to a dispute settlement officer designated by the state government, and (iii) appeal to the Contract Farming (Promotion and Facilitation) Authority (to be established in each state) in case they are not satisfied by the decision of the dispute settlement officer.

Stockholding limits on contracted produce

Stockholding limits are imposed through control orders as per the Essential Commodities Act, 1955. Such provisions of stockholding limits can be restrictive and discourage buyers to enter into contracts. It was recommended that the buyers can be exempted from stock limits up to six months of their requirement in the interest of trade. Under the draft Model Act, limits of stockholding of agricultural produce will not be applicable on produce purchased under contract farming.

Other recommendations

While contract farming seeks to provide alternative marketing channels and better price realisation to farmers, several other marketing reforms have been suggested by experts in this regard. These include: (i) allowing direct sale of produce by farmers, (ii) removing fruits and vegetables out of the ambit of APMCs, and (iii) setting-up of farmer-consumer markets, (iv) electronic trading, and (v) joining electronic National Agricultural Market for the sale of produce.

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